EMPLOYEE PLANS CPE TECHNICAL TOPICS FOR 2001

Current Developments-411(d)(6) regulations, electronic regs and other published guidance

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Section 411(d)(6) Regulations Special Rules Regarding Optional Forms of Benefit Under Qualified Retirement Plans

DATE: Wednesday, September 6, 2000

ACTION: Final regulations.

SUMMARY:

This document contains final regulations that permit qualified defined contribution plans to be amended to eliminate some alternative forms in which an account balance can be paid under certain circumstances, and permit certain transfers between defined contribution plans that were not permitted under prior final regulations. These regulations affect qualified retirement plan sponsors, administrators, and participants.

DATES: These regulations are effective September 6, 2000.

FOR FURTHER INFORMATION CONTACT: Linda S. F. Marshall, 202-622-6090 (not a toll-free number).

SUPPLEMENTARY INFORMATION:

Background

This document contains amendments to 26 CFR part 1 under section 411(d)(6) of the Internal Revenue Code of 1986 (Code).

Section 411(d)(6) generally provides that a plan will not be treated as satisfying the requirements of section 411 if the accrued benefit of a participant is decreased by a plan amendment. Section 411(d)(6)(B), which was added by the Retirement Equity Act of 1984 (REA), Public Law 98-397 (98 Stat. 1426), provides that a plan amendment that eliminates an optional form of benefit is treated as reducing accrued benefits to the extent that the amendment applies to benefits accrued as of the later of the adoption date or the effective date of the amendment. However, section 411(d)(6)(B) authorizes the Secretary of the Treasury to provide exceptions to this requirement. This authority

does not extend to a plan amendment that would [*53902] have the effect of eliminating or reducing an early retirement benefit or a retirement-type subsidy. Section 204(g)(2) of the Employee Retirement Income Security Act of 1974 (ERISA), Public Law 93-406 (88 Stat. 829), provides a parallel rule to section 411(d)(6)(B) of the Code that applies under Title I of ERISA, and authorizes the Secretary of the Treasury to provide exceptions to this parallel ERISA requirement. Thus, Treasury regulations issued under section 411(d)(6)(B) of the Code apply as well for purposes of section 204(g)(2) of ERISA.

Final regulations regarding section 411(d)(6)(B) (the 1988 regulations) were published in the **Federal Register** on July 8, 1988. The 1988 regulations, and subsequent amendments to the regulations, define the optional forms of benefit that are protected under section 411(d)(6)(B) and provide for certain exceptions to the general rule of section 411(d)(6)(B). In general, these regulatory exceptions to the application of section 411(d)(6)(B) to optional forms of benefit have been developed to address certain specific practical problems. For example, § 1.411(d)-4, Q&A-3(b) of the 1988 regulations permits a plan-to-plan transfer of a participant's entire nonforfeitable benefit to be made at the election of the participant, without a requirement that the transferee plan preserve all section 411(d)(6) protected benefits, but only if the participant is eligible to receive an immediate distribution and certain other conditions are satisfied. In addition, some regulatory exceptions to the application of section 411(d)(6)(B) to optional forms of benefit address plan amendments that are related to statutory changes. See Q&A-2(b) and Q&A-10 of § 1.411(d)-4.

The IRS and Treasury recognize that the accumulation of a variety of payment choices in a plan may increase the cost and complexity of plan operations. For example, an employer that initially adopted a plan for which the plan document was prepared by a prototype sponsor may now be using a different prototype plan that offers a different array of distribution forms. The requirement to preserve virtually all preexisting optional forms for benefits accrued up to the date of change in the prototype plan may present significant practical problems in certain cases. Similar issues arise where employers merge with or acquire other businesses. These employers often face issues of whether to maintain separate plans, terminate one or more of the plans, or merge the plans. If the employer chooses to merge the plans, the resulting plan may accumulate a wide variety of optional forms, some of which may differ in insignificant ways or may entail special administrative costs. Because the elective transfer rule of § 1.411(d)-4, Q&A-3(b) of the 1988 regulations has applied only to situations in which a participant's benefits have become distributable, its applicability has been limited.

In recent years, it has become easier for individuals to replicate the various payment choices available from qualified plans through other means. The Unemployment Compensation Amendments of 1992, Public Law 102-318 (106 Stat. 290), substantially expanded participants' ability to transfer distributions from qualified plans to individual retirement arrangements (IRAs) on a tax-deferred basis. Individuals who receive single-

sum distributions from qualified plans frequently roll those distributions over directly to IRAs, under which distributions can be made in a wide variety of payment forms. There are also indications that the vast majority of participants in defined contribution plans who are given a choice of distribution forms that includes a single-sum distribution elect the single-sum distribution.

The IRS and Treasury issued Notice 98-29 *(1998-1 C.B. 1163)* to request public comment on several ways of providing regulatory relief from the requirements of section 411(d)(6)(B) for defined contribution plans in view of these considerations. Most of the public comments received in response to Notice 98-29 indicated that, particularly for defined contribution plans, the section 411(d)(6)(B) requirement that a plan continue to offer all existing payment options often imposes significant administrative burdens that are disproportionate to any corresponding benefit to participants. After considering the comments received in response to Notice 98-29, the IRS and Treasury issued proposed regulations (REG-109101-98), which were published in the **Federal Register** *(65 FR 16546)* on March 29, 2000, to propose relief from the requirements of section 411(d)(6)(B) in a wide range of circumstances.

Seventeen written comments responding to the notice of proposed rulemaking were received. No public hearing was requested or held. Nearly all of the written comments expressed support for the provisions of the proposed regulation that would provide relief from the requirements of section 411(d)(6)(B) and requested clarifications or extensions of that relief in various ways. After consideration of all of the written comments, the IRS and the Treasury Department are adopting the proposed regulations as revised by this Treasury Decision for the reasons summarized below.

These final regulations under section 411(d)(6)(B) do not affect other requirements of the Code. For example, a money purchase pension plan (or a plan otherwise described in section 401(a)(11)(B)) generally must satisfy certain requirements relating to qualified joint and survivor annuities and qualified preretirement survivor annuities, and those requirements are not affected by these final regulations. Similarly, these final regulations do not affect the requirements of section 401(a)(31) relating to direct rollovers.

Explanation of Provisions

A. PERMITTED AMENDMENTS TO ALTERNATIVE FORMS OF PAYMENT UNDER A DEFINED CONTRIBUTION PLAN

In order to simplify plan administration, these final regulations adopt a modified version of the rule set forth in the proposed regulations that significantly expands the permitted changes that may be made to alternative forms of payment under a defined

contribution plan. Under the rule in the proposed regulations, a defined contribution plan would not violate the requirements of section 411(d)(6) merely because the plan was amended to eliminate or restrict the ability of a participant to receive payment of the participant's accrued benefit under a particular optional form of benefit if, after the plan amendment became effective with respect to the participant, the distribution choices available to the participant included both payment of the accrued benefit in a single-sum distribution form and payment of the accrued benefit in an extended payment form (such as, for example, an annuity distribution), each of which was otherwise identical to the eliminated or restricted optional form of benefit. In the preamble to the proposed regulations, the IRS and the Treasury Department requested comments on whether an extended payment form should be required to be preserved as part of such a plan amendment, or should be required to be preserved in particular circumstances.

In general, comments stated that the rule set forth in the proposed regulations would simplify plan administration. However, most commentators also indicated that requiring the retention of an extended payment form would perpetuate administrative burdens that would not be justified by any comparative advantage to plan participants. These [*53903] commentators pointed out various administrative burdens associated with retaining an extended payment form, such as maintaining a system to administer the extended payment form for the few (if any) participants who choose that payment form, including descriptions of the extended payment form in participant materials, explaining the extended payment form in response to participant inquiries, dealing with participant requests to accelerate distributions under the extended payment form, complying with the minimum required distribution rules of section 401(a)(9), and handling the problems that result from an increased incidence of missing participants. These commentators also pointed out the special burdens that maintenance of an extended payment option imposes in mergers and acquisitions. These commentators took the position that, in light of a participant's ability to roll over distributions to one or more IRAs, which commonly offer a far wider array of alternative payment forms, and in light of the ability of many participants to choose to retain their full vested account balance in the qualified plan, there is little or no advantage to the participant in rules requiring the plan sponsor to retain an option to receive extended payments from a qualified defined contribution plan.

After considering these comments regarding the desirability of requiring the retention of an extended payment form, and in light of the ability of participants to replicate any extended payment form that a defined contribution plan may offer by rolling over a single-sum distribution to an IRA, the IRS and the Treasury Department have determined that any advantages of requiring the retention of an extended payment form are outweighed by the countervailing considerations. Accordingly, these final regulations generally provide that a defined contribution plan does not violate the requirements of section 411(d)(6) merely because the plan is amended to eliminate or restrict the ability of a participant to receive payment of accrued benefits under a particular optional form of benefit if, after the plan amendment is effective with respect

to the participant, the alternative forms of payment available to the participant include payment in a single-sum distribution form that is otherwise identical to the optional form of benefit that is being eliminated or restricted. The final regulations adopt the rules set forth in the proposed regulations for determining whether a single-sum distribution is otherwise identical to an optional form of benefit that is being eliminated or restricted.

However, the final regulations include a provision that protects participants taking distributions shortly after the plan is amended, who may have planned on the availability of the payment form that is being eliminated or restricted. Under this provision, a plan amendment that eliminates or restricts the ability of a participant to receive a particular optional form of benefit cannot apply to any distribution that has an annuity starting date earlier than the 90th day n1 after the date the participant receiving the distribution has been furnished a summary that reflects the amendment and that satisfies the requirements of the Labor Department regulations at 29 CFR 2520.104b-3 relating to a summary of material modifications for pension plans (or, if earlier, the first day of the second plan year following the plan year in which the amendment is adopted).

n1 This 90-day requirement is parallel to the 90-day election period applicable to any plan that is subject to the joint and survivor annuity requirements of section 417.

As noted above, the final regulations do not affect the survivor annuity requirements of sections 401(a)(11) and 417 or the direct rollover requirements of section 401(a)(31).

One commentator expressed concern that permitting plan amendments that eliminate alternative forms of payment would have the effect of permitting the elimination of subsidized early retirement benefits (*i.e.,* distribution forms available upon early retirement that have a higher actuarial value than the normal retirement benefit that has been accrued at the time the distribution begins). These regulations, however, permit plan amendments eliminating alternative forms of payment only in certain circumstances involving defined contribution plans. Under a defined contribution plan, a participant is entitled to a distribution, in whatever form may be provided under the plan, only to the extent of the participant's individual account, plus earnings thereon. Accordingly, no alternative form of payment can be subsidized relative to any other payment form available under a defined contribution plan. Thus, these regulations do not have the effect of permitting the elimination of any early retirement subsidy or any other subsidized benefit forms.

B. VOLUNTARY DIRECT TRANSFERS BETWEEN PLANS

Under certain circumstances, the 1988 regulations permitted elimination of optional forms of benefit in connection with transfers of benefits from one plan to another with a participant's consent. See § 1.411(d)-4, Q&A-3(b) (as contained in 26 CFR part 1 revised April 1, 2000). The proposed regulations contained a number of changes to the 1988 regulations that would significantly liberalize the application of these elective

transfer provisions. These final regulations generally finalize the provisions of the proposed regulations relating to elective transfers, with certain modifications that are described below.

The 1988 regulations permitted an elective transfer from one qualified plan to another only if the participant's benefit under the transferring plan was immediately distributable (a distributable event transfer). This condition precluded use of the elective transfer provision in the 1988 regulations in connection with merger and acquisition transactions involving plans with a cash or deferred arrangement under section 401(k) in cases in which benefits under the cash or deferred arrangement were not distributable because section 401(k)(10) was not applicable. In response to Notice 98-29, many commentators stated that permitting elective transfers from the former employer's section 401(k) plan to the new employer's section 401(k) plan under these circumstances would allow employers to permit employees to keep their previously earned retirement benefits in a qualified plan together with their newly earned retirement benefits, particularly in cases where the new employer chooses not to maintain the former employer's plan.

Section 1.411(d)-4, Q&A-3(c) of these final regulations retains and modifies the previously applicable section 411(d)(6) relief for distributable event transfers, and § 1.411(d)-4, Q&A-3(b) of these final regulations adds new section 411(d)(6) relief for transfers in connection with certain corporate mergers and acquisitions or changes in the participant's employment status (transaction or employment change transfers). As a result, relief from section 411(d)(6) applies in each of the following cases:

- . *Direct rollover.* Existing rules provide that if a direct rollover is made from one qualified retirement plan to another, as described in section 401(a)(31), the receiving plan is not required by section 411(d)(6) to offer the same optional forms of benefit as the sending plan offered. See § 1.401(a)(31)-1, Q&A-14.
- . *Distributable event transfer.* As discussed further below, in any case in [*53904] which a participant is entitled to a distribution from either a defined benefit plan or a defined contribution plan but the participant is not eligible to receive an immediate distribution of the participant's entire nonforfeitable accrued benefit in a single-sum distribution that can be entirely rolled over, these final regulations provide section 411(d)(6) relief for a voluntary transfer. Thus, these regulations modify the distributable event transfer provisions of the 1988 regulations.
- . *Transaction or employment change transfer.* As discussed further below, even if a participant is not entitled to a distribution to which the preceding rules would apply, these final regulations, like the proposed regulations, allow a voluntary transfer from a defined contribution plan to another defined contribution plan of the same type if the transfer occurs in connection with a corporate merger or acquisition or a change in the participant's employment status. See § 1.411(d)-4, Q&A-3(b).

Under certain circumstances, it may be possible to accomplish a voluntary transfer of a participant's benefit from one defined contribution plan to another that could be structured as either a distributable event transfer or a transaction or employment change transfer. In such a situation, the plans would be required to comply with the requirements applicable to either one of those sets of rules with respect to the transfer.

1. *Expansion of Section 411(d)(6) Relief for Distributable Event Transfers*

Under section 401(a)(31), which was enacted after the issuance of the 1988 regulations, any eligible rollover distribution may be directly rolled over to an IRA or to another eligible retirement plan. The section 411(d)(6) requirements do not apply to amounts that have been distributed, including distributions that are directly rolled over to another plan under section 401(a)(31). Accordingly, for amounts that are distributable in an eligible rollover distribution, the elective transfer rules of the 1988 regulations have largely been duplicated by the enactment of section 401(a)(31) because the same section 411(d)(6) result generally is available through a direct rollover. These final regulations generally eliminate this duplication. Under these final regulations, for transfers occurring on or after January 1, 2002, the distributable event transfer rules are not available if the participant is eligible to receive an immediate distribution of the participant's entire nonforfeitable accrued benefit in a single-sum distribution that would consist entirely of an eligible rollover distribution within the meaning of section 401(a)(31)(C). (Instead, the plan must offer a section 401(a)(31) direct rollover.) However, in other situations, including situations in which a single-sum distribution is not available or the participant's benefit includes an amount attributable to after-tax employee contributions, the distributable event transfer rules will be available.

Some commentators requested that plans have the ability to characterize a transfer that could be accomplished totally or in part as a direct rollover under section 401(a)(31) as a direct transfer to which section 411(d)(6) relief applies. They point out that this procedure is permitted under the 1988 regulations and that this procedure would simplify plan administration. These final regulations clarify that plans are not required to bifurcate a transaction into a partial section 401(a)(31) direct rollover and a partial elective transfer to which section 411(d)(6) relief applies, but that plans are permitted, as an alternative to bifurcation, to treat such a transaction entirely as an elective transfer to which section 411(d)(6) relief applies. However, as noted above, for transfers occurring on or after January 1, 2002, this section 411(d)(6) relief for distributable event transfers does not apply to an elective transfer that occurs at a time at which the participant is eligible to receive an immediate distribution of the participant's entire nonforfeitable account balance in a single-sum distribution that would consist entirely of an eligible rollover distribution within the meaning of section 401(a)(31)(C). Instead, a similar result could be achieved by means of a direct rollover to which section 401(a)(31) applies.

Under the proposed regulations, the section 411(d)(6) relief for transfers of immediately distributable amounts other than eligible rollover distributions would only have applied to transfers between plans of the same type (*i.e.,* transfers from defined benefit plans to defined benefit plans and transfers from defined contribution plans to defined contribution plans), notwithstanding that the 1988 regulations granted section 411(d)(6) relief to transfers between plans of different types (*i.e.,* transfers from defined benefit plans to defined contribution plans and vice versa). The preamble specifically requested comments on whether section 411(d)(6) relief was needed for distributable event transfers between different types of plans, given the availability of direct rollovers. Several commentators stated that this section 411(d)(6) relief provided under the 1988 regulations was still valuable and also requested clarification that the relief applied to transfers of amounts that were immediately distributable only in the form of periodic payments commencing immediately. These final regulations adopt both of these recommendations.

2. Section 411(d)(6) Relief for Transaction or Employment Change Transfers

Section 1.411(d)-4, Q&A-3(b) of these final regulations retains and, in some respects, expands provisions of the proposed regulations that grant, subject to certain conditions, broad section 411(d)(6) relief for many types of elective transfers of a participant's entire benefit under a defined contribution plan, whether or not the benefit is immediately distributable (and whether or not the participant would be eligible for a distribution of the participant's entire benefit in a single-sum distribution that would be an eligible rollover distribution). In order to ensure that the participant's election occurs in connection with an independent event (and is not, in effect, a mere waiver), the transfer must be made either in connection with certain corporate transactions (such as a merger or acquisition) or in connection with a participant's change in employment status (for example, the participant's transfer to a different subsidiary or division of the employer, without regard to whether the transfer constitutes a separation from service) to an employment status with respect to which the participant is not entitled to additional allocations under the transferor plan, even if the event is not one that triggers the right to an immediate distribution. Such elective transfers can be made to a plan that is outside the employer's controlled group, to another plan of the same employer, or to a plan that is maintained by another member of the employer's controlled group.

A transaction or employment change transfer may involve benefits that are not fully vested under the transferor plan. However, where a participant's benefit that is not fully vested under the transferor plan is transferred pursuant to these rules, the vesting schedule amendment requirements of section 411(a)(10) must be satisfied.

A transaction or employment change transfer generally is only permitted between defined contribution plans of the same type (*e.g.,* from a qualified cash or deferred arrangement under section 401(k) to another qualified cash or deferred arrangement).

The restrictions on the types of plans [*53905] between which transaction or employment change transfers are permitted facilitate administration of the qualified plan distribution rules by ensuring that amounts transferred to the receiving plan, in a transfer that is not itself a distribution, will be subject to similar legal restrictions with respect to in-service distributions. See *Rev. Rul. 94-76 (1994-2 C.B. 46).* In the case of transfers from plans that are subject to the survivor annuity requirements of sections 401(a)(11)(A) and 417, those survivor annuity requirements would in any event apply to the receiving plan with respect to the transferred amount as a result of the transferee plan rule of section 401(a)(11)(B)(iii)(III).

In response to comments, the final regulations clarify that the right to a transaction or employment change transfer is an other right or feature for purposes of section 401(a)(4) (unlike a distributable event transfer, which is treated as an optional form of benefit for purposes of section 401(a)(4)). In applying section 401(a)(4) to a transaction or employment change transfer right, the final regulations permit certain conditions to be disregarded. Thus, for example, section 401(a)(4) would be satisfied if, with respect to all participants: (1) The plan provides a transfer right in the event that an employee ceases to be covered by the plan because of any asset or stock disposition, merger or other similar business transaction involving a change of the employer; (2) the plan provides a transfer right in the event that an employee ceases to be covered by the plan because of an identified asset or stock disposition, merger or other similar business transaction that involves a change of the employer; or (3) the plan provides a transfer right in the event that an employee ceases to be covered by the plan because of a transfer of employment to a position covered by another plan within the employer's controlled group.

C. RULES REGARDING IN-KIND DISTRIBUTIONS

The final regulations clarify and modify the rules regarding the application of the protections of section 411(d)(6)(B) to a right to receive benefit distributions in kind from defined contribution plans and defined benefit plans. Provisions for distribution in kind are sometimes found, for example, in plans invested in annuity contracts or in marketable mutual funds. The right to a particular form of investment is not a protected optional form of benefit. However, the investments made by a plan generally are subject to fiduciary requirements, including the prudence requirement of section 404(a)(1)(B) of ERISA. The 1988 regulations state that the right to a medium of distribution, such as cash or in-kind payments, is an optional form of benefit to which section 411(d)(6)(B) applies.

The proposed regulations provided that, if a defined benefit plan included an optional form of benefit under which benefits were distributed in the medium of an annuity

contract, that optional form of benefit could be modified by substituting cash for the annuity contract. The proposed regulations separately provided a similar rule for defined contribution plans that provided an annuity optional form of benefit and for distribution of an annuity contract, and that substituted a non-annuity optional form of benefit for the annuity form. These final regulations combine and simplify these two rules. The final regulations clarify that a participant's right to receive a particular benefit in the form of cash payments from either a defined benefit plan or a defined contribution plan and a participant's right to receive that benefit in the form of the distribution of an annuity contract that provides for cash payments that are otherwise identical in all respects to those cash payments from the plan are not separate optional forms of benefit. Therefore, for example, if a plan includes an optional form of benefit under which benefits are distributed in the medium of an annuity contract that provides for cash payments, that optional form of benefit may be modified by a plan amendment that substitutes cash payments from the plan for the distribution of the annuity contract, where those cash payments from the plan are identical to the cash payments payable from the annuity contract in all respects except for the source of the payments. Of course, a defined contribution plan that continues to offer a life annuity form of distribution must purchase an annuity contract from an insurance carrier in order to provide that optional form (and the plan may either distribute that contract to the participant or hold the contract as a plan asset from which it makes the payments for the participant).

These final regulations permit a defined contribution plan to be amended to replace the ability to receive a distribution in the form of marketable securities (other than employer securities) with the ability to receive a distribution in the form of cash. Thus, the right to distributions from a defined contribution plan in the form of cash, employer securities or other property that is not marketable securities is generally protected. The protection for employer securities reflects the potential value of the special tax treatment provided to net unrealized appreciation (NUA) on employer securities under section 402(e)(4). The protection for assets that are not marketable securities reflects that possibility that a participant may assign a higher value to such assets than the plan without the participant having the ability to acquire the asset after receiving a cash distribution.

The proposed regulations would permit a defined contribution plan that gives a participant the right to an in-kind distribution (including employer securities and property that is not marketable securities) to be amended to limit the types of property in which distributions can be made to a participant to specific types of property allocated to the participant's account at the time of the amendment (and with respect to which the participant had the right to receive an in-kind distribution before the plan amendment). In addition, the proposed regulations would permit a defined contribution plan giving a participant the right to a distribution in a type of property to be amended to specify that the participant is permitted to receive a distribution in that type of property only to the

extent that the plan assets allocated to the participant's account at the time of the distribution include that type of property.

These provisions of the proposed regulations were supported by commentators and have been adopted in these final regulations. In response to commentator suggestions, the examples from the proposed regulations have been modified in these regulations to clarify that a plan amendment that limits the right of a distribution in specified types of property to certain participants, as permitted by these regulations, need not itself contain a list of those participants. These provisions of the final regulations do not permit a plan to be amended in a way that affects protected features of optional forms of benefit other than the medium of distribution.

Effective Date and Applicability Date

These final regulations are effective September 6, 2000. These final regulations apply to plan amendments that are adopted and effective on or after September 6, 2000, except as provided in § 1.411(d)-4, Q&A-2(e)(1)(ii) and Q&A-3(c)(1)(ii).

Special Analyses

It has been determined that this Treasury decision is not a significant regulatory action as defined in Executive Order 12866. Therefore, a [*53906] regulatory assessment is not required. It also has been determined that section 553(b) of the Administrative Procedure Act *(5 U.S.C. chapter 5)* does not apply to these regulations, and because the regulation does not impose a collection of information on small entities, the Regulatory Flexibility Act *(5 U.S.C. chapter 6)* does not apply. Pursuant to section 7805(f) of the Code, the notice of proposed rulemaking preceding these regulations was submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on its impact on small business.

Drafting Information: The principal author of these regulations is Linda S. F. Marshall of the Office of the Division Counsel/Associate Chief Counsel (Tax Exempt and Government Entities). However, other personnel from the IRS and Treasury participated in their development.

List of Subjects in 26 CFR Part 1

Income taxes, Reporting and recordkeeping requirements.

Amendments to the Regulations

Accordingly, 26 CFR part 1 is amended as follows:

Paragraph 1. The authority citation for part 1 continues to read in part as follows:

Authority: *26 U.S.C. 7805 * * **

Par. 2. Section 1.411(d)-4 is amended as follows:

1. **In Q&A-1, paragraph (b)(1), the last sentence is amended by removing the language "§ 1.401(a)(4)-4(d)" and adding "§ 1.401(a)(4)-4(e)(1)" in its place.**
2. **Q&A-2 is amended by:**
   a. **In paragraph (a)(1), removing the language "in paragraph (b) of this Q&A-2" and adding the language "in this section" in its place.**
   b. **Adding two sentences at the beginning of paragraph (a)(3)(ii)(A).**
   c. **Revising the second sentence of paragraph (b)(2) introductory text.**
   d. **Revising paragraph (b)(2)(iii).**
   e. **Amending paragraph (b)(2)(viii) by removing the language " of the employer".**
   f. **Adding paragraph (e).**
3. **Q&A-3 is amended by:**
   a. **Revising paragraph (a)(3).**
   b. **Adding paragraph (a)(4).**
   c. **Revising paragraphs (b), (c), and (d).**

The additions and revisions read as follows:

§ 1.411(d)-4 -- Section 411(d)(6) protected benefits (Specific Amendments).

* * * * *

A-2: * * *(AMENDING A-2(A), (B), AND (C)

(A) * * *

(3) * * *

(ii) *Annuity contracts-*

(A) *General rule.* The right of a participant to receive a benefit in the form of cash payments from the plan and the right of a participant to receive that benefit in the form of the distribution of an annuity contract that provides for cash payments that are identical in all respects to the cash payments from the plan except with respect to the source of the payments are not separate optional forms of benefit. Therefore, for example, if a plan includes an optional form of benefit under which benefits are distributed in the medium of an annuity contract that provides for cash payments, that optional form of benefit may be modified by a plan amendment that substitutes cash payments from the plan for the annuity contract, where those cash payments from the plan are identical to the cash payments payable from the annuity contract in all respects except with respect to the source of the payments. * * *

* * * * *

(B) * * *

(2) * * * The rules with respect to permissible eliminations and reductions provided in this paragraph (b)(2) generally are effective January 30, 1986; however, the rules of paragraphs (b)(2)(iii) (A) and (B) and (b)(2)(viii) of this Q&A-2 are effective for plan amendments that are adopted and effective on or after September 6, 2000. * * *

* * * * *

(iii) *In-kind distributions* –

(A) *In-kind distributions payable under defined contribution plans in the form of marketable securities other than employer securities.* If a defined contribution plan includes an optional form of benefit under which benefits are distributed in the form of marketable securities, other than securities of the employer, that optional form of benefit may be modified by a plan amendment that substitutes cash for the marketable securities as the medium of distribution. For purposes of this paragraph (b)(2)(iii)(A) and paragraph (b)(2)(iii)(B) of this Q&A-2, the term *marketable securities* means marketable securities as defined in section 731(c)(2), and the term *securities of the employer* means securities of the employer as defined in section 402(e)(4)(E)(ii).

(B) *Amendments to defined contribution plans to specify medium of distribution.*

If a defined contribution plan includes an optional form of benefit under which benefits are distributable to a participant in a medium other than cash, the plan may be amended to limit the types of property in which distributions may be made to the participant to the types of property specified in the amendment. For this purpose, the types of property specified in the amendment must include all types of property

(other than marketable securities that are not securities of the employer) that are allocated to the participant's account on the effective date of the amendment and in which the participant would be able to receive a distribution immediately before the effective date of the amendment if a distributable event occurred. In addition, a plan amendment may provide that the participant's right to receive a distribution in the form of specified types of property is limited to the property allocated to the participant's account at the time of distribution that consists of property of those specified types.

(C) *In-kind distributions after plan termination.* If a plan includes an optional form of benefit under which benefits are distributed in specified property, that optional form of benefit may be modified for distributions after plan termination by substituting cash for the specified property as the medium of distribution to the extent that, on plan termination, an employee has the opportunity to receive the optional form of benefit in the form of the specified property. This exception is not available, however, if the employer that maintains the terminating plan also maintains another plan that provides an optional form of benefit under which benefits are distributed in the specified property.

(D) *Examples.* The following examples illustrate the application of this paragraph (b)(2)(iii):

Example 1.

(i) An employer maintains a profit-sharing plan under which participants may direct the investment of their accounts. One investment option available to participants is a fund invested in common stock of the employer. The plan provides that the participant has the right to a distribution in the form of cash upon termination of employment. In addition, the plan provides that, to the extent a participant's account is invested in the employer stock fund, the participant may receive an in-kind distribution of employer stock upon termination of employment. On October 18, 2000, the plan is amended, effective on January 1, 2001, to remove the fund invested in employer common stock as an investment option under the plan and to provide for the stock held in the fund to be sold. The amendment permits participants to elect how the sale proceeds are to be reallocated among the remaining investment options, and provides for amounts not so reallocated as of January 1, 2001, to be allocated to a specified investment option. [*53907]

(ii) The plan does not fail to satisfy section 411(d)(6) solely on account of the plan amendment relating to the elimination of the employer stock investment option, which is not a section 411(d)(6) protected benefit. See paragraph (d)(7) of Q&A-1 of this section. Moreover, because the plan did not provide for

distributions of employer securities except to the extent participants' accounts were invested in the employer stock fund, the plan is not required operationally to offer distributions of employer securities following the amendment. In addition, the plan would not fail to satisfy section 411(d)(6) on account of a further plan amendment, effective after the plan has ceased to provide for an employer stock fund investment option (and participants' accounts have ceased to be invested in employer securities), to eliminate the right to a distribution in the form of employer stock. See paragraph (b)(2)(iii)(B) of this Q&A-2.

Example 2.

(i) An employer maintains a profit-sharing plan under which a participant, upon termination of employment, may elect to receive benefits in a single-sum distribution either in cash or in kind. The plan's investments are limited to a fund invested in employer stock, a fund invested in XYZ mutual funds (which are marketable securities), and a fund invested in shares of PQR limited partnership (which are not marketable securities).

(ii) The following alternative plan amendments would not cause the plan to fail to satisfy section 411(d)(6):

(A) plan amendment that limits non-cash distributions to a participant on termination of employment to a distribution of employer stock and shares of PQR limited partnership. See paragraph (b)(2)(iii)(A) of this Q&A-2.

(B) A plan amendment that limits non-cash distributions to a participant on termination of employment to a distribution of employer stock and shares of PQR limited partnership, and that also provides that only participants with employer stock allocated to their accounts as of the effective date of the amendment have the right to distributions in the form of employer stock, and that only participants with shares of PQR limited partnership allocated to their accounts as of the effective date of the amendment have the right to distributions in the form of shares of PQR limited partnership. To comply with the plan amendment, the plan administrator retains a list of participants with employer stock allocated to their accounts as of the effective date of the amendment, and a list of participants with shares of PQR limited partnership allocated to their accounts as of the effective date of the amendment. See paragraphs (b)(2)(iii) (A) and (B) of this Q&A-2.

(C) A plan amendment that limits non-cash distributions to a participant on termination of employment to a distribution of employer stock and shares of PQR limited partnership to the extent that those assets are allocated to the participant's account at the time of the distribution. See paragraphs (b)(2)(iii) (A) and (B) of this Q&A-2.

(D) A plan amendment that limits non-cash distributions to a participant on termination of employment to a distribution of employer stock and shares of PQR limited partnership, and that provides that only participants with employer stock allocated to their accounts as of the effective date of the amendment have the right to distributions in the form of employer stock, and that only participants with shares of PQR limited partnership allocated to their accounts as of the effective date of the amendment have the right to distributions in the form of shares of PQR limited partnership, and that further provides that the distribution of that stock or those shares is available only to the extent that those assets are allocated to those participants' accounts at the time of the distribution. To comply with the plan amendment, the plan administrator retains a list of participants with employer stock allocated to their accounts as of the effective date of the amendment, and a list of participants with shares of PQR limited partnership allocated to their accounts as of the effective date of the amendment. See paragraphs (b)(2)(iii) (A) and (B) of this Q&A-2.

Example 3.

(i) An employer maintains a stock bonus plan under which a participant, upon termination of employment, may elect to receive benefits in a single-sum distribution in employer stock. This is the only plan maintained by the employer under which distributions in employer stock are available. The employer decides to terminate the stock bonus plan.

(ii) If the plan makes available a single-sum distribution in employer stock on plan termination, the plan will not fail to satisfy section 411(d)(6) solely because the optional form of benefit providing a single-sum distribution in employer stock on termination of employment is modified to provide that such distribution is available only in cash. See paragraph (b)(2)(iii)(C) of this Q&A-2.

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(E) PERMITTED PLAN AMENDMENTS AFFECTING ALTERNATIVE FORMS OF PAYMENT UNDER DEFINED CONTRIBUTION PLANS –

(1) *General rule.* A defined contribution plan does not violate the requirements of section 411(d)(6) merely because the plan is amended to eliminate or restrict the ability of a participant to receive payment of accrued benefits under a particular optional form of benefit if-

(i) After the plan amendment is effective with respect to the participant, the alternative forms of payment available to the participant include payment in a single-sum distribution form that is otherwise identical to the optional form of benefit that is being eliminated or restricted; and

(ii) The amendment does not apply to the participant with respect to any distribution with an annuity starting date that is earlier than the earlier of-

(A) The 90th day after the date the participant has been furnished a summary that reflects the amendment and that satisfies the requirements of 29 CFR 2520.104b-3 (relating to a summary of material modifications) for pension plans; or

(B) The first day of the second plan year following the plan year in which the amendment is adopted.

(2) *Otherwise identical single-sum distribution.*

For purposes of this paragraph (e), a single-sum distribution form is otherwise identical to an optional form of benefit that is eliminated or restricted pursuant to paragraph (e)(1) of this Q&A-2 only if the single-sum distribution form is identical in all respects to the eliminated or restricted optional form of benefit (or would be identical except that it provides greater rights to the participant) except with respect to the timing of payments after commencement. For example, a single-sum distribution form is not otherwise identical to a specified installment form of benefit if the single-sum distribution form is not available for distribution on the date on which the installment form would have been available for commencement, is not available in the same medium of distribution as the installment form, or imposes any condition of eligibility that did not apply to the installment form. However, an otherwise identical distribution form need not retain rights or features of the optional form of benefit that is eliminated or restricted to the extent that those rights or features would not be protected from elimination or restriction under section 411(d)(6) or this section.

(3) *Examples.* The following examples illustrate the application of this paragraph (e):

Example 1.

(i) P is a participant in Plan M, a qualified profit-sharing plan with a calendar plan year that is invested in mutual funds. The distribution forms available to P under Plan M include a distribution of P's vested account balance under Plan M in the form of distribution of various annuity contract forms (including a single life annuity and a joint and survivor annuity). The annuity payments under the annuity contract forms begin as of the first day of the month following P's termination of employment (or as of the first day of any subsequent month, subject to the requirements of section 401(a)(9)). P has not previously elected payment of benefits in the form of a life annuity, and Plan M is not a direct or indirect transferee of any plan that is a defined benefit plan or a defined contribution plan that is subject to section 412. Plan M provides that distributions on the death of a participant are made in accordance with section 401(a)(11)(B)(iii)(I). On May 15, 2001, Plan M is amended so that, after the amendment is effective, P is no longer entitled to any distribution in the form of the distribution of an annuity contract. However, after the amendment is effective, P is entitled to receive a single-sum cash distribution of P's vested account balance under Plan M payable as of the first day of [*53908] the month following P's termination of employment (or as of the first day of any subsequent month, subject to the requirements of section 401(a)(9)). The amendment does not apply to P if P elects to have annuity payments begin before the earlier of January 1, 2003, or 90 days after the date on which the plan administrator of Plan M furnishes P with a summary that reflects the amendment and that satisfies the requirements of 29 CFR 2520.104b-3. On December 14, 2001, the plan administrator of Plan M furnishes P with a summary plan description that reflects the amendment and that satisfies the requirements of 29 CFR 2520.104b-3.

(ii) Plan M does not violate the requirements of section 411(d)(6) (or section 401(a)(11)) merely because, as of March 14, 2002, the plan amendment has eliminated P's option to receive a distribution in any of the various annuity contract forms previously available.

Example 2.

(i) P is a participant in Plan M, a qualified profit-sharing plan to which section 401(a)(11)(A) does not apply. Upon termination of employment, P is entitled to receive cash distributions from Plan M, payable as of the first day of the month following P's termination of employment (or as of the first day of any subsequent month, subject to the requirements of section 401(a)(9)), in the form of a single-sum distribution, or in substantially equal monthly installment payments over either 5, 10, 15, or 20 years. On May 15, 2001, Plan M is

amended so that, after the amendment is effective, P is no longer entitled to receive a distribution in the form of substantially equal monthly installment payments over 5, 10, 15, or 20 years. However, after the amendment is effective, P continues to be entitled to receive cash distributions from Plan M, payable as of the first day of the month following P's termination of employment (or as of the first day of any subsequent month, subject to the requirements of section 401(a)(9)), in the form of a single-sum distribution. The amendment does not apply to P if P elects to have annuity payments begin before January 1, 2002. On September 20, 2001, the plan administrator of Plan M furnishes P with a summary of material modifications that reflects the amendment and that satisfies the requirements of 29 CFR 2520.104b-3.

(ii) Plan M does not violate the requirements of section 411(d)(6) merely because, as of January 1, 2002, the plan amendment has eliminated P's option to receive a distribution in the form of substantially equal monthly installment payments over 5, 10, 15, or 20 years.

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(4) *Effective date*. This paragraph (e) applies to plan amendments that are adopted on or after September 6, 2000.

* * * * *

A-3. (A) * * *(AMENDING A-3(A), (B), AND (C))

(3) *Waiver prohibition.*

In general, except as provided in paragraph (b) of this Q&A-3, a participant may not elect to waive section 411(d)(6) protected benefits. Thus, for example, the elimination of the defined benefit feature of a participant's benefit under a defined benefit plan by reason of a transfer of such benefits to a defined contribution plan pursuant to a participant election, at a time when the benefit is not distributable to the participant, violates section 411(d)(6).

(4) *Direct rollovers.*

A direct rollover described in Q&A-3 of § 1.401(a)(31)-1 that is paid to a qualified plan is not a transfer of assets and liabilities that must satisfy the requirements of section 414(l), and is not a transfer of benefits for purposes of applying the requirements under section 411(d)(6) and paragraph (a)(1) of this Q&A-3. Therefore,

for example, if such a direct rollover is made to another qualified plan, the receiving plan is not required to provide, with respect to amounts paid to it in a direct rollover, the same optional forms of benefit that were provided under the plan that made the direct rollover. See § 1.401(a)(31)-1, Q&A-14.

(B) ELECTIVE TRANSFERS OF BENEFITS BETWEEN DEFINED CONTRIBUTION PLANS –

(1) *General rule.*

A transfer of a participant's entire benefit between qualified defined contribution plans (other than any direct rollover described in Q&A-3 of § 1.401(a)(31)-1) that results in the elimination or reduction of section 411(d)(6) protected benefits does not violate section 411(d)(6) if the following requirements are met-

(i) *Voluntary election.* The plan from which the benefits are transferred must provide that the transfer is conditioned upon a voluntary, fully-informed election by the participant to transfer the participant's entire benefit to the other qualified defined contribution plan. As an alternative to the transfer, the participant must be offered the opportunity to retain the participant's section 411(d)(6) protected benefits under the plan (or, if the plan is terminating, to receive any optional form of benefit for which the participant is eligible under the plan as required by section 411(d)(6)).

(ii) *Types of plans to which transfers may be made.* To the extent the benefits are transferred from a money purchase pension plan, the transferee plan must be a money purchase pension plan. To the extent the benefits being transferred are part of a qualified cash or deferred arrangement under section 401(k), the benefits must be transferred to a qualified cash or deferred arrangement under section 401(k). To the extent the benefits being transferred are part of an employee stock ownership plan as defined in section 4975(e)(7), the benefits must be transferred to another employee stock ownership plan. Benefits transferred from a profit-sharing plan other than from a qualified cash or deferred arrangement, or from a stock bonus plan other than an employee stock ownership plan, may be transferred to any type of defined contribution plan.

(iii) *Circumstances under which transfers may be made.* The transfer must be made either in connection with an asset or stock acquisition, merger, or other similar transaction involving a change in employer of the employees of a trade or business (*i.e.*, an acquisition or disposition within the meaning of §

1.410(b)-2(f)) or in connection with the participant's change in employment status to an employment status with respect to which the participant is not entitled to additional allocations under the transferor plan.

(2) *Applicable qualification requirements.*

A transfer described in this paragraph (b) is a transfer of assets or liabilities within the meaning of section 414(l)(1) and, thus, must satisfy the requirements of section 414(l). In addition, this paragraph (b) only provides relief under section 411(d)(6); a transfer described in this paragraph must satisfy all other applicable qualification requirements. Thus, for example, if the survivor annuity requirements of sections 401(a)(11) and 417 apply to the plan from which the benefits are transferred, as described in this paragraph (b), but do not otherwise apply to the receiving plan, the requirements of sections 401(a)(11) and 417 must be met with respect to the transferred benefits under the receiving plan. In addition, the vesting provisions under the receiving plan must satisfy the requirements of section 411(a)(10) with respect to the amounts transferred.

(3) *Status of elective transfer as other right or feature.*

A right to a transfer of benefits from a plan pursuant to the elective transfer rules of this paragraph (b) is an other right or feature within the meaning of § 1.401(a)(4)-4(e)(3), the availability of which is subject to the nondiscrimination requirements of section 401(a)(4) and § 1.401(a)(4)-4. However, for purposes of applying the rules of § 1.401(a)(4)-4, the following conditions are to be disregarded in determining the employees to whom the other right or feature is available-

(i) A condition restricting the availability of the transfer to benefits of participants who are transferred to a different employer in connection with a specified asset or stock disposition, merger, or other similar transaction involving a change in employer of the employees of a trade or business (*i.e.*, a disposition within the meaning of § 1.410(b)-2(f)), or in connection with any such disposition, merger, or other similar transaction. [*53909]

(ii) A condition restricting the availability of the transfer to benefits of participants who have a change in employment status to an employment status with respect to which the participant is not entitled to additional allocations under the transferor plan.

(C) ELECTIVE TRANSFERS OF CERTAIN DISTRIBUTABLE BENEFITS BETWEEN QUALIFIED PLANS –

(1) *In general.* A transfer of a participant's benefits between qualified plans that results in the elimination or reduction of section 411(d)(6) protected benefits does not violate section 411(d)(6) if-

(i) The transfer occurs at a time at which the participant's benefits are distributable (within the meaning of paragraph (c)(3) of this Q&A-3);

(ii) For a transfer that occurs on or after January 1, 2002, the transfer occurs at a time at which the participant is not eligible to receive an immediate distribution of the participant's entire nonforfeitable accrued benefit in a single-sum distribution that would consist entirely of an eligible rollover distribution within the meaning of section 401(a)(31)(C);

(iii) The voluntary election requirements of paragraph (b)(1)(i) of this Q&A-3 are met;

(iv) The participant is fully vested in the transferred benefit in the transferee plan;

(v) In the case of a transfer from a defined contribution plan to a defined benefit plan, the defined benefit plan provides a minimum benefit, for each participant whose benefits are transferred, equal to the benefit, expressed as an annuity payable at normal retirement age, that is derived solely on the basis of the amount transferred with respect to such participant; and

(vi) The amount of the benefit transferred, together with the amount of any contemporaneous section 401(a)(31) direct rollover to the transferee plan, equals the entire nonforfeitable accrued benefit under the transferor plan of the participant whose benefit is being transferred, calculated to be at least the greater of the single-sum distribution provided for under the plan for which the participant is eligible (if any) or the present value of the participant's accrued benefit payable at normal retirement age (calculated by using interest and mortality assumptions that satisfy the requirements of section 417(e) and subject to the limitations imposed by section 415).

(2) *Treatment of transfer* –

(i) *In general.* A transfer of benefits pursuant to this paragraph (c) generally is treated as a distribution for purposes of section 401(a). For example, the transfer is subject to the cash-out rules of section 411(a)(7), the early termination requirements of section 411(d)(2), and the survivor annuity requirements of sections 401(a)(11) and 417. A transfer pursuant to the elective transfer rules of this paragraph (c) is not treated as a distribution for purposes of the minimum distribution requirements of section 401(a)(9).

(ii) *Status of elective transfer as optional form of benefit.* A right to a transfer of benefits from a plan pursuant to the elective transfer rules of this paragraph (c) is an optional form of benefit under section 411(d)(6), the availability of which is subject to the nondiscrimination requirements of section 401(a)(4) and § 1.401(a)(4)-4.

(3) *Distributable benefits.*

For purposes of paragraph (c)(1)(i) of this Q&A-3, a participant's benefits are distributable on a particular date if, on that date, the participant is eligible, under the terms of the plan from which the benefits are transferred, to receive an immediate distribution of these benefits (*e.g.*, in the form of an immediately commencing annuity) from that plan under provisions of the plan not inconsistent with section 401(a).

(d) *Effective date.* This Q&A-3 is applicable for transfers made on or after September 6. 20000.

* * * * *

Robert E. Wenzel,

Deputy Commissioner of Internal Revenue.

Approved: August 28, 2000.

Jonathan Talisman,

Acting Assistant Secretary of the Treasury.

Rev. Rul. 2000-36 Qualified plan- default rollover; involuntary cash-out (with no 411(d)(6) violation)

Section 411.--Minimum Vesting Standards

26 CFR 1.411(d)-4: Section 411(d)(6) protected benefits.

(Also, § 401; § 1.401(a)(31)-1.)

July 31, 2000

This ruling provides that if plan participants are given adequate notice including their right to elect a cash distribution, a qualified plan can be amended to permit a default direct rollover under section 401(a)(31) of an involuntary cash-out without there being a violation of section 411(d)(6) of the Code.

ISSUE

Will an amendment to change the default method of payment to a direct rollover for involuntary distributions when a distributee fails affirmatively to elect to make a direct rollover or to elect a cash payment under the facts described below cause the plan to fail to satisfy § 401(a)(31) or § 411(d)(6) of the Internal Revenue Code?

FACTS

Employer X maintains Plan A, a qualified defined contribution plan that does not include any after-tax contributions or other amounts that would not be included in gross income upon distribution. Plan A provides for an involuntary distribution to an employee upon separation from service if his or her vested account balance is $ 5,000 or less. Plan A includes a direct rollover option for all distributions. Plan A provides that if a separating employee's vested account balance is $ 5,000 or less, and the separating employee does not elect a direct rollover either to another qualified plan or to an individual retirement arrangement ("IRA"), the vested account balance is to be paid in a single sum cash payment to the employee.

Employer X amends Plan A to provide that the default form of payment of any involuntary cash-out from Plan A greater than $ 1,000 but less than or equal to $ 5,000 will be a direct rollover (an eligible rollover distribution that is paid directly to an eligible

retirement plan for the benefit of the distributee) to an IRA, but that separating employees will instead receive a cash payment if they so elect. Under the amendment, this default direct rollover applies only if the separating employee fails to request affirmatively

(1) a cash payment to that employee or

(2) a direct rollover to another qualified plan or an IRA designated by the separating employee.

The amendment also provides that in the case of a default direct rollover, the plan administrator will select21 an IRA trustee, custodian, or issuer (the "trustee") that is unrelated to Employer X, establish the IRA with that trustee on behalf of any separating employee who fails affirmatively to elect a direct rollover or a cash payment, and make the initial investment choices for the account.

The administrative procedures of Plan A are changed with respect to any § 402(f) notice provided on or after the effective date of the amendment to a separating employee with a vested account balance greater than $ 1,000 but not greater than $ 5,000. After the change, the plan administrator will include with the § 402(f) notice an explanation, as required by § 1.401(a)(31)-1 of the Income Tax Regulations, of the default direct rollover (and other appropriate information such as the name, address, and telephone number of the IRA trustee and information regarding IRA maintenance and withdrawal fees and how the IRA funds will be invested). The default direct rollover will occur not less than 30 days and not more than 90 days after the § 402(f) notice with the explanation of the default direct rollover is provided to the separating employee.

LAW AND ANALYSIS

21 The Department of Labor (the "DOL") has advised Treasury and the Service that, under Title I of the Employee Retirement Income Security Act ("ERISA"), in the context of a default direct rollover described in this ruling, where the distribution constitutes the entire benefit rights of the participant, the participant will cease to be a participant covered under the plan within the meaning of 29 CFR § 2510.3-3(d)(2)(ii)(B), and the distributed assets will cease to be plan assets within the meaning of 29 CFR § 2510.3-101. The DOL also noted that the selection of an IRA trustee, custodian or issuer and IRA investment for purposes of a default direct rollover would constitute a fiduciary act subject to the general fiduciary standards and prohibited transaction provisions of ERISA. In addition, plan provisions governing the default direct rollover of distributions, including the participant's ability to affirmatively opt out of the arrangement, must be described in the plan's summary plan description furnished to participants and beneficiaries.

Section 401(a)(31) provides, in part, that a trust shall not constitute a qualified trust unless the plan of which the trust is a part provides that if the distributee of any eligible rollover distribution (i) elects to have the distribution paid to an eligible retirement plan, and (ii) specifies the eligible retirement plan to which the distribution is to be paid, the distribution will be paid in a direct rollover to the eligible retirement plan specified.

Section 402(f) requires a plan administrator, within a reasonable period of time before making an eligible rollover distribution from an eligible retirement plan, to provide to the recipient a written explanation of the rollover provisions of § 401(a)(31) and § 402(c) (direct rollover and 60-day rollover), the 20-percent mandatory withholding requirement under § 3405, and other tax provisions in § 402 that apply to the eligible rollover distribution.

Section 411(d)(6)(A) provides, in part, that a plan participant's accrued benefit may not be decreased by a plan amendment other than by an amendment described in § 412(c)(8) of the Code or § 4281 of the Employee Retirement Income Security Act of 1974. Section 411(d)(6)(B) provides that an amendment eliminating or reducing an optional form of benefit is treated as an amendment reducing an employee's accrued benefit unless otherwise provided in Income Tax Regulations.

Section 1.401(a)(31)-1, Q&A-7 provides, in part, that a plan administrator may establish a default procedure so that if a distributee fails to make an affirmative election, he or she is treated as having made a direct rollover election. However, that regulation requires the plan administrator to first furnish the distributee with an explanation of the default procedure and an explanation of the direct rollover option within the time period provided in § 1.402(f)-1, Q&A-2 for the written explanation described in § 402(f).

Section 1.402(f)-1, Q&A-1 prescribes the general rule with respect to the contents of the written explanation (§ 402(f) notice) that must be provided to a distributee by a plan administrator before an eligible rollover distribution is made. Section 1.402(f)-1, Q&A-2 provides generally that the plan administrator must provide a distributee of an eligible rollover distribution with a § 402(f) notice no less than 30 days and no more than 90 days before the date of the distribution. Although a participant may, under the circumstances described in § 1.402(f)-1, Q&A-2, affirmatively elect to receive a distribution before the expiration of the 30 days after the receipt of a § 402(f) notice, that rule would not apply to a default direct rollover.

Section 1.411(d)-4, Q&A-1(a) defines a "section 411(d)(6) protected benefit" as a benefit described in § 411(d)(6)(A), early retirement benefits and retirement-type subsidies described in § 411(d)(6)(B)(i), and optional forms of benefit described in § 411(d)(6)(B)(ii) and provides that those benefits, to the extent that they are accrued, are subject to the protections of § 411(d)(6).

The default status of an optional form of benefit is not a section 411(d)(6) protected benefit. Thus, an amendment to change Plan A's default method of payment for an involuntary distribution from a direct cash payment to a direct rollover does not violate § 411(d)(6). As required in § 1.401(a)(31)-1, Q&A-7, Plan A's procedures provide that each distributee subject to the default will receive an explanation of the default procedure and the direct rollover option within a time period before the default direct rollover that satisfies the timing requirements of § 1.402(f)-1, Q&A-2. Thus, the provision of a direct rollover as the default method of payment under the facts described above does not cause Plan A to fail to satisfy § 401(a)(31).

HOLDING

An amendment to change the default method of payment to a direct rollover as the default when a distributee fails affirmatively to elect to make a direct rollover or to elect a cash payment under the facts described above does not cause Plan A to fail to satisfy § 401(a)(31) or § 411(d)(6).

DRAFTING INFORMATION

The principal author of this revenue ruling is Michael Rubin of the Tax Exempt and Government Entities Division. For further information regarding this revenue ruling, call the Employee Plans' taxpayer assistance telephone service at (202) 622-6074/6075 (not toll-free numbers) between 1:30 and 3:30 p.m.

Eastern Time, Monday through Thursday. Mr. Rubin's telephone number is (202) 622-6214 (also not a toll-free call).

Announcement 2000-71

Amendment of Qualified Plans for Final Regulations Under § 411(d)(6)

October 13, 2000

Final regulations under § 411(d)(6) of the Code were published in the Federal Register on September 6, 2000. The regulations grant relief under § 411(d)(6) by permitting qualified defined contribution plans to be amended, under certain conditions, to eliminate some alternative forms of payment and to eliminate or limit the right to receive certain in-kind distributions. The final regulations also permit certain transfers between plans that were not previously permitted. The regulations generally apply to amendments adopted, and transfers made, on or after September 6, 2000.

Effective September 6, 2000, plan sponsors may adopt plan amendments that are permitted under the final regulations under § 411(d)(6). Determination letters that are issued with respect to plans for which an application is filed with the Service on or after September 6, 2000, may be relied upon with respect to whether a plan satisfies the requirements of the final regulations.

Some plans might contain language that would necessitate a change to conform to the final regulations (as described below). Such a plan must be amended, in connection with its application for a determination letter, to satisfy the final regulations. See below regarding the effective date of the amendment.

Plan sponsors that have determination letter applications on file with the Service which were submitted before September 6, 2000, should contact the Service if they wish to amend their plans and have the provisions of the final regulations taken into account in their determination letters. Plan sponsors should contact the EP specialist who has been assigned to review their application, if possible. Otherwise, they should contact Customer Service on 1-877-829-5500. In these cases, the Service will try to accommodate the plan sponsor's request to have the provisions of the final regulations taken into account in the determination letter. However, if the EP specialist assigned to review the application has already completed that review, the Service will not be able to accommodate the plan sponsor's request and a new application and user fee will be required.

In general, the final regulations expand the permitted changes that may be made to alternative forms of payment and in-kind distributions under a defined contribution plan and, in the case of voluntary direct transfers between plans, the circumstances under which elimination of optional forms of benefit is permitted. Generally, therefore, plan

sponsors may choose to amend their plans as a result of these changes, but are not required to do so, except as provided below.

The regulations under § 411(d)(6), as in effect prior to September 6, 2000, ("the 1988 regulations") permitted elimination of optional forms of benefit in connection with voluntary direct transfers between plans, provided certain requirements were satisfied. Section 401(a)(31), which was added after the 1988 regulations, requires that participants be able to elect a direct rollover to an IRA or other eligible retirement plan of any eligible rollover distribution. Because the requirements of § 411(d)(6) do not apply to amounts distributed, including those amounts directly rolled over under § 401(a)(31), the voluntary direct transfer rules in the 1988 regulations produce the same § 411(d)(6) result with respect to an eligible rollover distribution as a direct rollover under § 401(a)(31).

The final regulations under § 411(d)(6) generally eliminate this duplication. The final regulations provide, in part, that relief from the requirements of § 411(d)(6) is not available under the voluntary transfer rules where the participant is entitled to elect a § 401(a)(31) direct rollover because the participant is eligible to receive an immediate distribution of the participant's entire nonforfeitable accrued benefit in a single-sum distribution that would consist entirely of an eligible rollover distribution within the meaning of § 401(a)(31)(C). This provision of the final regulations is effective for transfers occurring on or after January 1, 2002.

Some plans might contain pre-existing provisions that permit elimination of optional forms of benefit pursuant to the voluntary direct transfer rules as in effect under the 1988 regulations. To the extent that these plan provisions are inconsistent with the final regulations under § 411(d)(6), as described in the preceding paragraph, the plan must be amended. The amended plan must provide that the benefit of a participant described in the preceding paragraph may be voluntarily transferred only through a § 401(a)(31) direct rollover.

Any plan amendment required to conform the plan terms to the final § 411(d)(6) regulations does not have to be adopted prior to the end of the plan's GUST remedial amendment period, as described in Rev. Proc. 2000-27, 2000-26 I.R.B. 1272, and Rev. Proc. 2000-20, 2000-6 I.R.B. 553. However, as provided above, if a determination letter application for the plan is filed on or after September 6, 2000, the required plan amendment must be adopted in connection with the application. In any case, the plan amendment must be effective no later than January 1, 2002.

Final Regulations-New Technologies in Retirement Plans

DATE: Tuesday, February 8, 2000

ACTION: Final regulations.

SUMMARY:

This document contains amendments to the regulations governing certain notices and consents required in connection with distributions from retirement plans. Specifically, these regulations set forth applicable standards for the transmission of those notices and consents through electronic media and modify the timing requirements for providing certain distribution-related notices. The regulations provide guidance to plan sponsors and administrators by interpreting the notice and consent requirements in the context of the electronic administration of retirement plans. The regulations affect retirement plan sponsors, administrators, and participants.

DATES: Effective Date: These regulations are effective January 1, 2001.

Applicability Date: These regulations apply to plan years beginning on or after January 1, 2001.

FOR FURTHER INFORMATION CONTACT: Catherine Livingston Fernandez, (202) 622-6030 (not a toll-free number).

SUPPLEMENTARY INFORMATION:

Paperwork Reduction Act

The collection of information contained in these final regulations has been reviewed and approved by the Office of Management and Budget in accordance with the Paperwork Reduction Act (44 U.S.C. 3507) under control number 1545-1632. Responses to this collection of information are mandatory.

An agency may not conduct or sponsor, and a person is not required to respond to, a collection of information unless the collection of information displays a valid control number.

The estimated annual burden per respondent and/or recordkeeper is 76 minutes.

Comments concerning the accuracy of this burden estimate and suggestions for reducing this burden should be sent to the Internal Revenue Service, Attn: IRS Reports Clearance Officer, OP:FS:FP, Washington, DC 20224, and to the Office of Management and Budget, Attn: Desk Officer for the Department of the Treasury, Office of Information and Regulatory Affairs, Washington, DC 20503.

Books or records relating to this collection of information must be retained as long as their contents may become material in the administration of any internal revenue law. Generally, tax returns and tax return information are confidential, as required by 26 U.S.C. 6103.

Background

This document contains amendments to the Income Tax Regulations (26 CFR parts 1 and 35) under sections 402(f), 411(a)(11) and 3405(e)(10)(B). The regulations under section 3405(e)(10)(B) (new Q/A d-35 and d-36 of section 35.3405-1), like the regulations under sections 402(f) and 411(a)(11) are final regulations. These regulations finalize proposed regulations that were published as a notice of proposed rulemaking (REG-118662-98) in the Federal Register (63 FR 70071) on December 18, 1998. A public hearing was held on the proposed regulations on April 15, 1999.

In addition to the proposed regulations, the IRS and Treasury issued Notice 99-1 (1999-2 I.R.B. 8), and Announcement 99-6 (1999-4 I.R.B. 24), concerning the use of electronic media under retirement plans. Notice 99-1 confirms that the "paperless" administration of participant enrollments, contribution elections, investment elections, beneficiary designations (other than designations requiring spousal consent), direct rollover elections, and certain other transactions do not cause a qualified plan to fail to satisfy the requirements of section 401(a) (or the requirements for a qualified cash or deferred arrangement under section 401(k)). Announcement 99-6 authorizes the electronic transmission of Form W-4P.

The proposed regulations, Notice 99-1, and Announcement 99-6 were issued pursuant to section 1510 of the Taxpayer Relief Act of 1997. That section provides for the Secretary of the Treasury to issue guidance designed to interpret the notice, election, consent, disclosure, time, and related recordkeeping requirements under the Code and the Employee Retirement Income Security Act of 1974 (ERISA) regarding the

use of new technologies by sponsors and administrators of retirement plans and to clarify the extent to which writing requirements under the Code relating to retirement plans permit paperless transactions. Section 1510 provides that the guidance must protect participant and beneficiary rights. Any final regulations applicable to this guidance may not be effective until the first plan year beginning at least six months after issuance as final regulations.

Explanation of Provisions

General

Commentators generally praised the approach taken in the proposed regulations of providing broad, flexible standards for the transmission of certain notices and consent required for distributions through electronic media. Commentators stated that the guidelines set forth in the proposed regulations facilitate the expanded use of new technologies and recognize the likelihood of future technological advances in plan administration. Accordingly, the final regulations retain this approach and:

. Permit electronic delivery of the notice of distribution options and the right to defer distribution under section 411(a)(11), the rollover notice under section 402(f), and the withholding notice under section 3405(e)(10)(B); [*6002]

. Permit electronic transmission of participant consent to a distribution under section 411(a)(11); and

. Permit a plan to provide the section 411(a)(11) and section 402(f) notices more than 90 days before a distribution, if the plan provides a summary of the notices within 90 days before the distribution.

Notices Under Sections 402(f), 411(a)(11), and 3405(e)(10)(B)

1. USE OF ELECTRONIC MEDIA FOR DELIVERY OF NOTICES

The proposed regulations provide that, in general, a plan may furnish a notice required under section 402(f), 411(a)(11), or 3405(e)(10)(B) either on a written paper document or through an electronic medium reasonably accessible to the participant to whom the notice is given. The proposed regulations require that any electronic notice be provided under a system reasonably designed to give the notice in a manner no less

understandable to the participant than a written paper document and that the participant be advised of the right to request and to receive a copy of the notice on a written paper document without charge. The final regulations adopt these rules without change.

One commentator noted that the proposed regulations do not define the term reasonably accessible and suggested that the final regulations require that participants have effective access at their place of work to any electronic medium used to deliver the notices under sections 402(f), 411(a)(11), and 3405(e)(10)(B). The IRS and Treasury, after further consideration, believe that the reasonably accessible standard protects the interests of plan participants and, therefore, have retained the proposed terminology.

The same commentator raised more general concerns with the use of electronic media to transmit notices. This commentator argued that an electronic notice should be "actually received (not just sent or available) and read by the participant, be permanently accessible, and easily converted to a printed document, by using an available printer and/or through a request for a paper writing." In response to these concerns, the IRS and Treasury reiterate the view, expressed in the preamble to the proposed regulations, that the legal standards for the delivery of distribution-related notices under sections 402(f), 411(a)(11), and 3405(e)(10)(B) should be the same regardless of the medium of delivery. Additionally, the IRS and Treasury note that many of the concerns raised by this commentator about electronic media are adequately addressed by the requirement in the regulations that participants always have the right to request and to receive a written paper notice without charge.

Several commentators objected to the requirement that participants be able to receive the notice on a written paper document upon request. These commentators argued that simply making written paper notices available through an electronic medium (such as a printing option on an e-mail system or a plan web site) protects the interests of participants in having access to written paper notices without placing the burden of providing written paper notices on plan sponsors and administrators. However, the IRS and Treasury believe that the right to request and to receive a written paper notice is an important fail-safe for paperless plan administration. The requirement ensures that no participant is denied ready access to a usable copy of a required distribution notice, and it limits the need for the IRS and Treasury to regulate the manner in which written paper notices are made available through electronic media. The IRS and Treasury believe that the burden for plan sponsors and administrators to maintain a process that will generate written paper notices upon request is outweighed by the important safeguards provided by the requirement. In addition, as indicated in the preamble to the proposed regulations, the written paper notice provided on request need not be identical to the electronic notice. Therefore, the written paper notice can be either a printed version of the electronic notice or a separate notice prepared for distribution on paper. In light of these considerations, the requirement is retained in the final regulations.

One commentator requested clarification that the proposed regulations under section 3405 would permit the electronic delivery of the annual notice described in section 3405(e)(10)(B)(i)(III) (which is provided to recipients of periodic payments). The proposed regulations, as written, apply to that annual notice; however, the final regulations make this point expressly. One commentator asked that the proposed regulations be amended to provide for electronic withholding elections under section 3405 in addition to electronic transmission of notices under section 3405. It is unclear what, if any, utility such a change in the regulations would have in light of the ability to use electronic media for transmission of Form W-4P, as set out in Announcement 99-6. Therefore, no change has been made to the regulations on this point.

2. FLEXIBILITY FOR TIMING REQUIREMENT IN PROVIDING NOTICES

Commentators favored the provision in the proposed regulations that provided flexibility with respect to the 90-day period under sections 402(f) and 411(a)(11) by providing an alternative timing rule. Under this alternative timing rule, a plan may give the full section 402(f) and section 411(a)(11) notices more than 90 days before the distribution and provide the participant a summary of the notice during the 90/30-day period under those sections. The full notice is not required to be provided on a regular periodic basis and may be provided in connection with other materials (for example, in the summary plan description or in a brochure describing plan distribution features), but it must be updated (and provided to the participant) as necessary to ensure accuracy as of the time the summary is given. The proposed regulations provide that the summary notice must set out the principal provisions of the full notice, must refer the participant to the most recent occasion on which the full notice was provided, and must advise the participant of the right to request and to receive a copy of the full notice without charge.

Several commentators interpreted the requirement in the proposed regulations that the summary refer the participant to the most recent occasion on which the full notice was provided as requiring an indication of the precise date on which the participant was given the full notice and the precise location of the full notice if it was provided in a document containing other information (such as the summary plan description). These commentators argued that this information may vary on a participant-by-participant basis and so imposes a considerable administrative burden on plan sponsors and administrators22.

2222 For example, many plan sponsors provide a copy of the summary plan description to each employee when the employee is first hired. If the full notice is provided through the summary plan description, the precise date on which the full notice was last provided could differ for each participant.

The IRS and Treasury did not intend for the proposed regulations to be construed as requiring individualized information about the full notice. Therefore, the final regulations clarify, first, that the summary must refer participants to the most recent version of the full notice. The purpose of this rule is to minimize confusion among participants if more than one version of a full notice has been provided in the [*6003] past. In many of those cases, this reference could reasonably be made by calendar year (for example, by referring to the 1999 version of the section 402(f) notice). If more than one version of a distribution notice was provided in a single calendar year, more precise reference should be made (for example, by referring to the May 1999 version of the section 402(f) notice). Reference to the notice by month or year would not be necessary if only one version of the notice had been provided in the past. If the full notice were constantly available (for example, a notice that is available on a plan web site and is kept up-to-date), it would be adequate to state that fact.

Additionally, the regulations have been modified to provide that, in the case of a full notice provided in a document containing other information, the summary must identify that document and must provide a reasonable indication of where the notice may be found in the document. This requirement could be satisfied through a number of means, including identification of page number, section heading, an index reference, the title of the notice, or any other reference that would reasonably direct the participant to the notice.

One commentator objected to the alternative timing rule set out in the proposed regulations. This commentator argued that distribution-related notices should be tied to a specific event (such as a participant request for a distribu- tion) and that "it is inappropriate to provide a notice of the notice when using electronic or other new technologies when it is just as easy to provide the actual notice itself." The IRS and Treasury agree that the information contained in the section 402(f) and section 411(a)(11) notices should be provided to a participant in connection with the participant's contemplation of a distribution, but the IRS and Treasury believe that providing a summary of a previously provided notice and informing the participant of the right to request and to receive the full notice adequately protect the interests of participants in this regard.

The preamble to the proposed regulations includes an example of a summary section 402(f) notice provided through an automated telephone system. Many commentators raised questions about this example. Several commentators argued that the sample summary is too long and complex to be of use in plan administration; others argued that it does not include reference to every potentially applicable rule concerning the taxation of plan distributions (for example, it does not refer to the taxation of net unrealized appreciation on the distribution of employer securities). Commentators also inquired about the legal status of the example because of its placement in the preamble. The example was intended merely to illustrate a summary notice that, in the view of the IRS

and Treasury, satisfies the requirements of the proposed regulations. It was not intended as a model summary or as the exclusive form for such a summary. Although the example is not restated in these final regulations, the IRS and Treasury are considering whether to issue additional guidance providing additional examples of summary notices. In this regard, the IRS and Treasury will solicit comments from interested parties regarding the development of those examples and will invite interested parties to submit draft summary notices to assist in the development of that guidance.

Consent Under Section 411(a)(11)

Consistent with the proposed regulations, the final regulations provide that, in general, a plan may receive a participant's consent either on a written paper document or through an electronic medium reasonably accessible to the participant. As in the case of participant notices, the regulations generally do not categorize particular electronic media as either permissible or impermissible for this purpose and do not prescribe detailed, media-specific rules. The standards are intended to parallel the key attributes of participant consent provided on written paper documents without imposing more stringent requirements on electronic consents. The proposed regulations provide that participant consent transmitted through an electronic medium must be given under a system that is reasonably designed to preclude an individual other than the participant from giving the consent and that provides the participant a reasonable opportunity to review and to confirm, modify, or rescind the terms of the distribution before the consent to the distribution becomes effective. Comments on this portion of the proposed regulations were generally favorable, and no change has been made in the final regulations.

One commentator, however, objected outright to the use of electronic media for the transmission of participant consent and argued that, at a minimum, such consent "should not be effective until after a written confirmation is received and the participant has a specified amount of time to revoke it." This commentator also argued that the final regulations should prohibit the use of automated telephone systems to provide distribution-related notices and to receive participant consent unless an automatic, mandatory written confirmation of the participant's election of a distribution option is required along with a seven-day right of revocation. The IRS and Treasury concluded that it is not advisable to impose new revocation rules based on the medium through which a participant consents to a distribution. Both the proposed regulations and the final regulations require that the terms of any consent made through an electronic medium be confirmed to the participant. Additionally, the IRS and Treasury do not believe that a right of revocation for a defined period after consent is given is more necessary or appropriate in the case of consent made through an electronic medium than it is in the case of consent made through a written paper document. More

generally, the IRS and Treasury do not believe that the use of electronic media is improper or inappropriate for the transmission of a participant's consent under section 411(a)(11). If the requirements of the regulations are satisfied, consent provided in that manner should reflect the considered wishes of the participant as reliably as a consent provided through a written paper document.

Changes to the Examples in the Regulations

Several commentators expressed concern about details in the examples illustrating the proposed regulations for distribution notices and consent. One of the concerns involved the statement in the examples that a participant who wished to change a PIN electronically would be unable to proceed with a distribution transaction until the plan sent a confirmation of the change to the participant. Commentators stated that the electronic systems maintained by plan sponsors and administrators use an array of security features to ensure participant identity, some of which might permit an electronic transaction to proceed after a PIN change. Although the prohibition on proceeding with an electronic transaction after a PIN change was intended only to illustrate a commonly used system and not as a substantive requirement, the final regulations omit the statement from the examples for the sake of clarity. Of course, the examples in the final regulations presuppose that plan sponsors and administrators maintain adequate measures to ensure participant identity when a PIN is changed. [*6004]

Notice 99-1 and Announcement 99-6

Commentators expressed support for Notice 99-1, which indicates that a qualified plan will not fail to meet the requirements of section 401(a) (and that a qualified cash-or-deferred arrangement will not fail to meet the requirements of section 401(k)) merely because it permits a participant or beneficiary to use electronic media to effect a transaction for which no specific provision of the Code, the regulations, or other guidance of general applicability sets forth rules or standards regarding the media through which it may be conducted. Announcement 99-6 permits the electronic transmission of Form W-4P.

Commentators asked for clarification whether Form W-4P may be transmitted through a telephone system. The underlying standards for the electronic transmission of Form W-4P are intended to be the same as those for the electronic transmission of Form W-4, as set out in § 31.3402(f)(5)-1(c). The preamble to the proposed regulations for the electronic transmission of Form W-4 indicates that "[i]f an employer chooses to establish an electronic system, the employer will be free to determine the type of system (such as telephone or computer) or systems available to its employees." (59 FR 18508 (Apr. 15,

1994)). Therefore, the use of a telephone system for electronic transmission of Form W-4P, if otherwise consistent with Announcement 99-6 and § 31.3402(f)(5)-1(c), is permissible.

Commentators also asked the IRS and Treasury to reconsider the requirement, stated in Announcement 99-6, that the electronic signature on Form W-4P be the final entry in the submission of the form. These commentators argue that this effectively requires the participant in most cases to enter a PIN at both the beginning and the end of a transaction that involves the use of an electronic Form W-4P. The IRS and Treasury are considering this issue and anticipate issuing additional guidance on this question.

Scope of These Regulations

These regulations do not address the application of Title I of ERISA (except for section 203(e)) to the use of electronic media for any plan communication or transaction. Several commentators requested that the regulations be expanded to include matters not covered by the proposed regulations. Most notably, commentators asked that the IRS and Treasury provide guidance on the use of electronic media for plan loans under section 72(p), nondiscrimination safe-harbor notices under sections 401(k)(12) and 401(m)(11), notices under section 204(h) of ERISA, and distribution notices, elections, and spousal consents governed by sections 401(a)(11) and section 417.

The IRS and Treasury are actively considering comments submitted on regulations proposed under section 72(p) and expect to issue additional guidance under that section. It is anticipated that any guidance on the use of electronic media in connection with plan loans would be issued in connection with that additional guidance. As the IRS and Treasury have noted in the past, notices under sections 401(k)(12) and 401(m)(11) and ERISA section 204(h) present legal issues distinct from those presented by notices under sections 402(f), 411(a)(11), and 3405(e)(10)(B). Notice 2000-3 (2000-4 I.R.B.--) provides that, pending further guidance, notices under sections 401(k)(12) and 401(m)(11) may be issued through electronic media if standards set forth in Notice 2000-3 which are similar to those applicable to notices under these regulations, are satisfied. Because of the unique considerations applicable to notices under ERISA section 204(h), guidance with respect to the use of electronic media in connection with section 204(h) notices is not being issued at this time.

Finally, regarding notices, elections, and spousal consents governed by sections 401(a)(11) and section 417, the IRS and Treasury note that the statutory requirement that spousal consent be witnessed either by a notary public or a plan representative appears to presuppose that a spouse be in the physical presence of the notary public or the plan representative at the time consent is given. This appears to place significant

limitations on the utility of electronic media in effecting spousal consent. n2 Thus, it is unclear what guidance the IRS and Treasury could issue that would meaningfully facilitate paperless distributions in the case of plans subject to sections 401(a)(11) and 417.

n2 One commentator suggested that electronic transmission of spousal consent be permitted if the plan has "reasonable certainty that the spouse has consented." That suggested standard appears to fall far short of the witnessing requirement specifically set forth in the statute.

Reliance

Plan sponsors and administrators may rely on these final regulations for guidance for distributions made prior to the effective date.

Special Analyses

It has been determined that this Treasury decision is not a significant regulatory action as defined in Executive Order 12866. Therefore, a regulatory impact analysis is not required. It is hereby certified that these regulations will not have a significant economic impact on a substantial number of small entities. This certification is based on the fact that the regulations provide paperless alternatives to notices that otherwise must be sent as written paper documents. It is anticipated that most small businesses affected by these regulations will be sponsors of retirement plans. Since these notices are provided only upon distributions and since, in the case of a small plan, there will be relatively few distributions per year, small plans that implement a paperless system for delivering these notices will likely contract for them as part of a paperless system for distributions offered by outside vendors. The paperless delivery of the notices will not add more than a minor increment to the cost of these distribution systems or the plan sponsor will continue to use a paper-based system. Accordingly, a Regulatory Flexibility Analysis is not required. Pursuant to section 7805(f) of the Code, the notice of proposed rulemaking preceding these regulations was submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on its impact on small business.

Drafting Information

The principal author of these regulations is Catherine Livingston Fernandez, Office of the Associate Chief Counsel (Employee Benefits and Exempt Organizations), IRS. However, personnel from other offices of the IRS and Treasury Department participated in their development.

EMPLOYEE PLANS CPE TECHNICAL TOPICS FOR 2001

List of Subjects

26 CFR Part 1

Income taxes, Reporting and recordkeeping requirements.

26 CFR Part 35

Employment taxes, Income taxes, Reporting and recordkeeping requirements.

26 CFR Part 602

Reporting and recordkeeping requirements.

Amendments to the Regulations

Accordingly, 26 CFR parts 1, 35, and 602 are amended as follows: [*6005]

PART 1--INCOME TAXES-(Specific Amendments)

Paragraph 1. The authority citation for part 1 continues to read, in part, as follows:

Authority: 26 U.S.C. 7805 * * *

Par. 2. Section 1.402(f)-1 is amended by:

1. Revising Q&A-2.

2. Adding Q&A-5 and Q&A-6.

The revision and additions read as follows:

§ 1.402(F)--1 -- REQUIRED EXPLANATION OF ELIGIBLE ROLLOVER DISTRIBUTIONS; QUESTIONS AND ANSWERS.

* * * * *

Q-2: WHEN MUST THE PLAN ADMINISTRATOR PROVIDE THE SECTION 402(F) NOTICE TO A DISTRIBUTEE?

A-2: The plan administrator must provide the section 402(f) notice to a distributee at a time that satisfies either paragraph (a) or (b) of this Q&A-2.

(a) This paragraph (a) is satisfied if the plan administrator provides a distributee with the section 402(f) notice no less than 30 days and no more than 90 days before the date of a distribution. However, if the distributee, after having received the section 402(f) notice, affirmatively elects a distribution, a plan will not fail to satisfy section 402(f) merely because the distribution is made less than 30 days after the section 402(f) notice was provided to the distributee, provided the plan administrator clearly indicates to the distributee that the distributee has a right to consider the decision of whether or not to elect a direct rollover for at least 30 days after the notice is provided. The plan administrator may use any method to inform the distributee of the relevant time period, provided that the method is reasonably designed to attract the attention of the distributee. For example, this information could be either provided in the section 402(f) notice or stated in a separate document (e.g., attached to the election form) that is provided at the same time as the notice. For purposes of satisfying the requirement in the first sentence of paragraph (a) of this Q&A-2, the plan administrator may substitute the annuity starting date, within the meaning of § 1.401(a)-20, Q&A-10, for the date of the distribution.

(b) This paragraph (b) is satisfied if the plan administrator-

(1) Provides a distributee with the section 402(f) notice;

(2) Provides the distributee with a summary of the section 402(f) notice within the time period described in paragraph (a) of this Q&A-2; and

(3) If the distributee so requests after receiving the summary described in paragraph (b)(2) of this Q&A-2, provides the section 402(f) notice to the distributee without charge and no less than 30 days before the date of a distribution (or the annuity starting date), subject to the rules for the distributee's waiver of that 30-day period. The summary described in paragraph (b)(2) of this Q&A-2 must set forth a summary of the principal provisions of the section 402(f) notice, must refer the distributee to the most recent version of the section 402(f) notice (and, in the case of a notice provided in any document containing information in addition to the notice, must identify that document and must provide a reasonable indication of where the notice may be found in that document, such as by index reference or by

section heading), and must advise the distributee that, upon request, a copy of the section 402(f) notice will be provided without charge.

* * * * *

Q-5:

Will the requirements of section 402(f) be satisfied if a plan administrator provides a distributee with the section 402(f) notice or the summary of the notice described in paragraph (b)(2) of Q&A-2 of this section other than through a written paper document?

A-5: A plan administrator may provide a distributee with the section 402(f) notice or the summary of that notice described in paragraph (b)(2) of Q&A-2 of this section either on a written paper document or through an electronic medium reasonably accessible to the distributee. A notice or summary provided through an electronic medium must be provided under a system that satisfies the following requirements:

(a) The system must be reasonably designed to provide the notice or summary in a manner no less understandable to the distributee than a written paper document.

(b) At the time the notice or summary is provided, the distributee must be advised that the distributee may request and receive the notice on a written paper document at no charge, and, upon request, that document must be provided to the distributee at no charge.

Q-6: ARE THERE EXAMPLES THAT ILLUSTRATE THE PROVISIONS OF Q&A-2 AND Q&A-5 OF THIS SECTION?

A-6: The following examples illustrate the provisions of Q&A-2 and Q&A-5 of this section:

Example 1.

(i) A qualified plan (Plan A) permits participants to request distributions by e-mail. Under Plan A's system for such transactions, a participant must enter his or her account number and personal identification number (PIN); this information must match that in Plan A's records in order for the transaction to proceed. If a participant requests a distribution from Plan A by e-mail and the distribution is an eligible rollover distribution, the plan administrator provides the participant with a

section 402(f) notice by e-mail. The plan administrator also advises the participant that he or she may request the section 402(f) notice on a written paper document and that, if the participant requests the notice on a written paper document, it will be provided at no charge. To proceed with the distribution by e-mail, the participant must acknowledge receipt, review, and comprehension of the section 402(f) notice.

(ii) In Example 1, Plan A does not fail to satisfy the notice requirement of section 402(f) merely because the notice is provided to the participant other than through a written paper document.

Example 2.

(i) A qualified plan (Plan B) permits participants to request distributions through the Plan B web site (Internet or intranet). Under Plan B's system for such transactions, a participant must enter his or her account number and personal identification number (PIN); this information must match that in Plan B's records in order for the transaction to proceed. A participant may request a distribution from Plan B by following the applicable instructions on the Plan B web site. After the participant has requested a distribution that is an eligible rollover distribution, the participant is automatically shown a page on the web site containing a section 402(f) notice. Although this page of the web site may be printed, the page also advises the participant that he or she may request the section 402(f) notice on a written paper document by calling a telephone number indicated on the web page and that, if the participant requests the notice on a written paper document, it will be provided at no charge. To proceed with the distribution by e-mail, the participant must acknowledge receipt, review, and comprehension of the section 402(f) notice.

(ii) In this Example 2, Plan B does not fail to satisfy the notice requirement of section 402(f) merely because the notice is provided to the participant other than through a written paper document.

Example 3.

(i) (i) A qualified plan (Plan C) permits participants to request distributions through Plan C's automated telephone system. Under Plan C's system for such transactions, a participant must enter his or her account number and personal identification number (PIN); this information must match that in Plan C's records in order for the transaction to proceed. Plan C provides the section 402(f) notice in the summary plan description, the most recent version of which was distributed to participants in 1997. A participant may request a distribution from Plan C by

following the applicable instructions on the automated telephone system. In 1999, a participant, using Plan C's automated telephone system, requests a distribution that is an eligible rollover distribution. The automated telephone system refers the participant to the most recent version of the section 402(f) notice which was provided in the summary plan description, informs the participant where the section 402(f) notice [*6006] may be located in the summary plan description, and provides an oral summary of the material provisions of the section 402(f) notice. The system also advises the participant that the participant may request the section 402(f) notice on a written paper document and that, if the participant requests the notice on a written paper document, it will be provided at no charge. Before proceeding with the distribution, the participant must acknowledge receipt, review, and comprehension of the summary. Under Plan C's system for processing such transactions, the participant's distribution will be made no more than 90 days and no fewer than 30 days after the participant requests the distribution and receives the summary of the section 402(f) notice (unless the participant waives the 30-day period).

(ii) In this Example 3, Plan C does not fail to satisfy the notice requirement of section 402(f) merely because Plan C provides a summary of the section 402(f) notice or merely because the summary is provided to the participant other than through a written paper document.

Example 4.

(i) Same facts as Example 3, except that, pursuant to Plan C's system for processing such transactions, a participant who so requests is transferred to a customer service representative whose conversation with the participant is recorded. The customer service representative provides the summary of the section 402(f) notice by reading from a prepared text.

(ii) In this Example 4, Plan C does not fail to satisfy the notice requirement of section 402(f) merely because Plan C provides a summary of the section 402(f) notice or merely because the summary of the section 402(f) notice is provided to the participant other than through a written paper document.

Example 5.

(i) Same facts as Example 3, except that Plan C does not provide the section 402(f) notice in the summary plan description. Instead, the automated telephone system reads the section 402(f) notice to the participant.

(ii) In this Example 5, Plan C does not satisfy the notice requirement of section 402(f) because oral delivery alone of the section 402(f) notice through the automated telephone system is not sufficient.

Example 6.

(i) The facts are the same as in Example 1, except that Participant D requested a distribution by e-mail, then terminated employment, and, following the termination, no longer has reasonable access to Plan A e-mail.

(ii) In this Example 6, Plan A does not satisfy the notice requirement of section 402(f) because the electronic medium through which the notice is provided is not reasonably accessible to Participant D. Plan A must provide the section 402(f) notice to Participant D in a written paper document or by an electronic means that is reasonably accessible to Participant D.

Par. 3. Section 1.411(a)-11 is amended by:

1. Revising paragraphs (c)(2)(i) and (iii).

2. Removing the language "Written consent" in paragraph (c)(2)(ii) and (c)(3) and adding "Consent" in its place.

3. Adding paragraphs (f) and (g).

The revisions and additions read as follows:

Section 1.411(a)-11 -- Restriction and valuation of distributions.

* * * * *

(C) * * *

(2) Consent.

(i) No consent is valid unless the participant has received a general description of the material features of the optional forms of benefit available under the plan. In addition, so long as a benefit is immediately distributable, a participant must be informed of the right, if any, to defer receipt of the distribution. Furthermore,

consent is not valid if a significant detriment is imposed under the plan on any participant who does not consent to a distribution. Whether or not a significant detriment is imposed shall be determined by the Commissioner by examining the particular facts and circumstances.

* * * * *

(iii) A plan must provide a participant with notice of the rights specified in this paragraph (c)(2) at a time that satisfies either paragraph (c)(2)(iii)(A) or (B) of this section:

(A) This paragraph (c)(2)(iii)(A) is satisfied if the plan provides a participant with notice of the rights specified in this paragraph (c)(2) no less than 30 days and no more than 90 days before the date the distribution commences. However, if the participant, after having received this notice, affirmatively elects a distribution, a plan will not fail to satisfy the consent requirement of section 411(a)(11) merely because the distribution commences less than 30 days after the notice was provided to the participant, provided the plan administrator clearly indicates to the participant that the participant has a right to at least 30 days to consider whether to consent to the distribution.

(B) This paragraph (c)(2)(iii)(B) is satisfied if the plan-

(1) Provides the participant with notice of the rights specified in this paragraph (c)(2);

(2) Provides the participant with a summary of the notice within the time period described in paragraph (c)(2)(iii)(A) of this section; and

(3) If the participant so requests after receiving the summary described in paragraph (c)(2)(iii)(B)(2) of this section, provides the notice to the participant without charge and no less than 30 days before the date the distribution commences, subject to the rules for the participant's waiver of that 30-day period. The summary described in paragraph (c)(2)(iii)(B)(2) of this section must advise the participant of the right, if any, to defer receipt of the distribution, must set forth a summary of the distribution options under the plan, must refer the participant to the most recent version of the notice (and, in the case of a notice provided in any document containing information in addition to the notice, must identify that document and must provide a reasonable indication of where the notice may be found in that document, such as by index reference or by section heading), and must advise the participant that, upon request, a copy of the notice will be provided without charge.

* * * * *

(F) MEDIUM FOR NOTICE AND CONSENT –

(1) Notice. The notice of a participant's rights described in paragraph (c)(2) of this section or the summary of that notice described in paragraph (c)(2)(iii)(B)(2) of this section may be provided either on a written paper document or through an electronic medium reasonably accessible to the participant. A notice or summary provided through an electronic medium must be provided under a system that satisfies the following requirements:

(i) The system must be reasonably designed to provide the notice or summary in a manner no less understandable to the participant than a written paper document.

(ii) At the time the notice or summary is provided, the participant must be advised that he or she may request and receive the notice on a written paper document at no charge, and, upon request, that document must be provided to the participant at no charge.

(2) Consent. The consent described in paragraphs (c)(2) and (3) of this section may be given either on a written paper document or through an electronic medium reasonably accessible to the participant. A consent given through an electronic medium must be given under a system that satisfies the following requirements:

(i) The system must be reasonably designed to preclude any individual other than the participant from giving the consent.

(ii) The system must provide the participant with a reasonable opportunity to review and to confirm, modify, or rescind the terms of the distribution before the consent to the distribution becomes effective.

(iii) (iii) The system must provide the participant, within a reasonable time after the consent is given, a confirmation of the terms (including the form) of the distribution either on a written paper document or through an electronic medium under a system that [*6007] satisfies the requirements of paragraph (f)(1) of this section.

(G) EXAMPLES.

The provisions of paragraph (f) of this section are illustrated by the following examples:

Example 1.

(i) A qualified plan (Plan A) permits participants to request distributions by e-mail. Under Plan A's system for such transactions, a participant must enter his or her account number and personal identification number (PIN); this information must match that in Plan A's records in order for the transaction to proceed. If a participant requests a distribution from Plan A by e-mail, the plan administrator provides the participant with a section 411(a)(11) notice by e-mail. The plan administrator also advises the participant by e-mail that he or she may request the section 411(a)(11) notice on a written paper document and that, if the participant requests the notice on a written paper document, it will be provided at no charge. To proceed with the distribution by e-mail, the participant must acknowledge receipt, review, and comprehension of the section 411(a)(11) notice and must consent to the distribution within the time required under section 411(a)(11). Within a reasonable time after the participant's consent by e-mail, the plan administrator, by e-mail, sends confirmation of the terms (including the form) of the distribution to the participant and advises the participant that he or she may request the confirmation on a written paper document that will be provided at no charge.

(ii) In this Example 1, Plan A does not fail to satisfy the notice or consent requirement of section 411(a)(11) merely because the notice and consent are provided other than through written paper documents.

Example 2.

(i) Same facts as Example 1, except that, instead of sending a confirmation of the distribution by e-mail, the plan administrator, within a reasonable time after the participant's consent, sends the participant an account statement for the period that includes information reflecting the terms of the distribution.

(ii) In this Example 2, Plan A does not fail to satisfy the consent requirement of section 411(a)(11) merely because the consent is provided other than through a written paper document.

Example 3.

(i) A qualified plan (Plan B) permits participants to request distributions through the Plan B web site (Internet or intranet). Under Plan B's system for such transactions, a participant must enter his or her account number and personal identification number (PIN); this information must match that in Plan B's records in order for the transaction to proceed. A participant may request a distribution from Plan B by following the applicable instructions on the Plan B web site. After the participant has requested a distribution, the participant is automatically shown a page on the web site containing a section 411(a)(11) notice. Although this page of the web site may be printed, the page also advises the participant that he or she may request the section 411(a)(11) notice on a written paper document by calling a telephone number indicated on the web page and that, if the participant requests the notice on a written paper document, it will be provided at no charge. To proceed with the distribution by e-mail, the participant must acknowledge receipt, review, and comprehension of the section 411(a)(11) notice and must consent to the distribution within the time required under section 411(a)(11). The web site requires the participant to review and confirm the terms (including the form) of the distribution before the transaction is completed. After the participant has given consent via e-mail, the Plan B web site confirms the distribution to the participant and advises the participant that he or she may request the confirmation on a written paper document that will be provided at no charge.

(ii) In this Example 3, Plan B does not fail to satisfy the notice or consent requirement of section 411(a)(11) merely because the notice and consent are provided other than through written paper documents.

Example 4.

(i) A qualified plan (Plan C) permits participants to request distributions through Plan C's automated telephone system. Under Plan C's system for such transactions, a participant must enter his or her account number and personal identification number (PIN); this information must match that in Plan C's records in order for the transaction to proceed. Plan C provides only the following distribution options: a lump sum and annual installments over 5, 10, or 20 years. A participant may request a distribution from Plan C by following the applicable instructions on the automated telephone system. After the participant has requested a distribution, the automated telephone system reads the section 411(a)(11) notice to the participant. The automated telephone system also advises the participant that he or she may request the notice on a written paper document and that, if the participant requests the notice on a written paper document, it will be provided at no charge. Before proceeding with the distribution transaction, the participant must acknowledge receipt, review, and comprehension of the section 411(a)(11) notice and must consent to the

distribution within the time required under section 411(a)(11). The automated telephone system requires the participant to review and confirm the terms (including the form) of the distribution before the transaction is completed. After the participant has given consent, the automated telephone system confirms the distribution to the participant and advises the participant that he or she may request the confirmation on a written paper document that will be provided at no charge. Because Plan C has relatively few and simple distribution options, the provision of the section 411(a)(11) notice over the automated telephone system is no less understandable to the participant than a written paper notice.

(ii) In this Example 4, Plan C does not fail to satisfy the notice or consent requirement of section 411(a)(11) merely because the notice and consent are provided other than through written paper documents.

Example 5.

(i) Same facts as Example 4, except that, pursuant to Plan C's system for processing such transactions, a participant who so requests is transferred to a customer service representative whose conversation with the participant is recorded. The customer service representative provides the section 411(a)(11) notice from a prepared text and processes the participant's distribution in accordance with predetermined instructions of the plan administrator.

(ii) In this Example 5, Plan C does not fail to satisfy the notice or consent requirement of section 411(a)(11) merely because the notice and consent are provided other than through written paper documents.

Example 6.

(i) Same facts as Example 1, except that Participant D requested a distribution by e-mail, then terminated employment and, following the termination, no longer has access to e-mail.

(ii) In this Example 6, Plan A does not satisfy the notice or consent requirement of section 411(a)(11) because the electronic medium through which the notice is provided is not reasonably accessible to Participant D. Plan A must provide Participant D the section 411(a)(11) notice in a written paper document or by an electronic means that is reasonably accessible to Participant D.

Par. 4. The heading for part 35 is revised to read as follows:

PART 35--EMPLOYMENT TAX AND COLLECTION OF INCOME TAX AT SOURCE REGULATIONS UNDER THE TAX EQUITY AND FISCAL RESPONSIBILITY ACT OF 1982

Par. 5. The authority citation for part 35 is revised to read as follows:

Authority: 26 U.S.C. 6047(e), 7805; 68A Stat. 917; 96 Stat. 625; Public Law 97-248 (96 Stat. 623).

Section 35.3405-1 also issued under 26 U.S.C. 3405(e)(10)(B)(iii).

Section 35.3405-1T also issued under 26 U.S.C. 3405(e)(10)(B)(iii).

Par. 6. Redesignate § 35.3405-1T and revise the heading to read as follows:

Section 35.3405-1T -- Questions and answers relating to withholding on pensions, annuities, and certain other deferred income (temporary regulations).

* * * * *

Par. 7. A new § 35.3405-1 is added to read as follows:

§ 35.3405-1 -- Questions and answers relating to withholding on pensions, annuities, and certain other deferred income.

The following questions and answers relate to withholding on pensions, annuities, and other deferred income under section 3405 of the Internal Revenue Code of 1986, as added by section 334 of the Tax Equity and Fiscal Responsibility Tax Act of 1982 (Public Law 97-248) (TEFRA).

a-1 through d-34 [Reserved] For further guidance, see § 35.3405-1T. [*6008]

D-35. Q. THROUGH WHAT MEDIUM MAY A PAYOR PROVIDE THE NOTICE REQUIRED UNDER SECTION 3405 TO A PAYEE?

A. A payor may provide the notice required under section 3405 (including the abbreviated notice described in d-27 and the annual notice described in d-31) to a payee either on a written paper document or through an electronic medium reasonably

accessible to the payee. A notice provided through an electronic medium must be provided under a system that satisfies the following requirements:

(a) The system must be reasonably designed to provide the notice in a manner no less understandable to the payee than a written paper document.

(b) At the time the notice is provided, the payee must be advised that the payee may request and receive the notice on a written paper document at no charge, and, upon request, that document must be provided to the payee at no charge.

D-36. Q. ARE THERE EXAMPLES THAT ILLUSTRATE THE PROVISIONS OF D-35 OF THIS SECTION?

A. The provisions of d-35 of this section are illustrated by the following examples:

Example 1.

(i) An employer deferred compensation plan (Plan A) permits participants to request distributions by e-mail. Under Plan A's system for such transactions, a participant must enter his or her account number and personal identification number (PIN); this information must match that in Plan A's records in order for the transaction to proceed. The plan administrator is the payor. If a participant requests a distribution from Plan A by e-mail, the plan administrator provides the participant with the notice required under section 3405 by e-mail. The plan administrator also advises the participant by e-mail that he or she may request the notice on a written paper document and that, if the participant requests the notice on a written paper document, it will be provided at no charge. To proceed with the distribution by e-mail, the participant must acknowledge receipt, review, and comprehension of the notice.

(ii) In this Example 1, the plan administrator does not fail to satisfy the notice requirement of section 3405 merely because the notice is provided to the participant other than through a written paper document.

Example 2.

(i) An employer deferred compensation plan (Plan B) permits participants to request distributions through the Plan B web site (Internet or intranet). Under Plan B's system for such transactions, a participant must enter his or her account number

and personal identification number (PIN); this information must match that in Plan B's records in order for the transaction to proceed. The plan administrator is the payor. A participant may request a distribution from Plan B by following the applicable instructions on the Plan B web site. After the participant has requested a distribution, the participant is automatically shown a page on the web site containing the notice required by section 3405. Although this page of the web site may be printed, the page also advises the participant that he or she may request the notice on a written paper document and that, if the participant requests the notice on a written paper document, it will be provided at no charge. To proceed with the distribution through the web site, the participant must acknowledge receipt, review, and comprehension of the notice.

(ii) In this Example 2, the plan administrator does not fail to satisfy the notice requirement of section 3405 merely because the notice is provided to the participant other than through a written paper document.

Example 3.

(i) An employer deferred compensation plan (Plan C) permits participants to request distributions through Plan C's automated telephone system. Under Plan C's system for such transactions, a participant must enter his or her account number and personal identification number (PIN); this information must match that in Plan C's records in order for the transaction to proceed. The plan administrator is the payor. A participant may request a distribution from Plan C by following the applicable instructions on the automated telephone system. After the participant has requested a distribution, the automated telephone system reads the notice required by section 3405 to the participant. The automated telephone system also advises the participant that he or she may request the notice on a written paper document and that, if the participant requests the notice on a written paper document, it will be provided at no charge. Before proceeding with the distribution transaction, the participant must acknowledge receipt, review, and comprehension of the notice.

(ii) In this Example 3, the plan administrator does not fail to satisfy the notice requirement of section 3405 merely because the notice is provided to the participant other than through a written paper document.

Example 4.

(i) Same facts as Example 3, except that, pursuant to the system for processing such transactions, a participant who so requests is transferred to a customer service representative whose conversation with the participant is recorded. The

customer service representative provides the notice required by section 3405 by reading from a prepared text.

(ii) Conclusion. In this Example 4, the plan administrator does not fail to satisfy the notice requirement of section 3405 merely because the notice is provided to the participant other than through a written paper document.

Example 5.

(i) Same facts as Example 1, except that Participant D requested a distribution by e-mail and then terminated employment. Participant D no longer has access to e-mail.

(ii) In this Example 5, Plan A does not satisfy the notice requirement of section 3405 because the electronic medium through which the notice is provided is not reasonably accessible to Participant D. Plan A must provide the notice required by section 3405 to Participant D in a written paper document or by an electronic medium that is reasonably accessible to Participant D.

PART 602--OMB CONTROL NUMBERS UNDER THE PAPERWORK REDUCTION ACT

Par. 6. The authority citation for part 602 continues to read as follows:

Authority: 26 U.S.C. 7805.

Par. 7. In § 602.101, paragraph (b) is amended by adding the following entry in the table in numerical order to read as follows:

§ 602.101 -- OMB Control numbers.

* * * * *

(b) * * *

CFR part or section where identified and described	Current OMB control No.
* * * * *	
1.402(f)-1	1545-1632

* * * * *

1.411(a)-11 1545-1632

* * * * *

Robert E. Wenzel,

Deputy Commissioner of Internal Revenue.

Approved: January 20, 2000.

Jonathan Talisman,

Acting Assistant Secretary of the Treasury.

[FR Doc. 00-1897 Filed 2-7-00; 8:45 am]

BILLING CODE 4830-01-U

Rev. Proc. 2000-17 (Waiver of 4971(b) for certain terminating plans)

26 CFR 601.201: Rulings and determination letters.

(Also Part I, §§ 412, 4971.)

March 13, 2000

Section 1. Purpose

This revenue procedure provides for a waiver of the 100 percent tax imposed under § 4971(b) of the Internal Revenue Code (the "Code") on an employer who maintains a pension plan for which there is an accumulated funding deficiency under § 412. The waiver is applicable to certain terminated single-employer defined benefit plans if specific conditions are satisfied.

Section 2. Background

.01 Section 4971(a) provides for the imposition of an initial tax of ten percent (five percent in the case of a multiemployer plan) on the amount of the accumulated funding deficiency under a plan as determined under § 412.

.02 Section 4971(b) provides for an additional tax equal to 100 percent of any uncorrected accumulated funding deficiency on which an initial tax is imposed under § 4971(a).

.03 Section 3002(b) of the Employee Retirement Income Security Act of 1974 ("ERISA"), Pub. L. 93-406, 1974-3 C.B. 166, provides that the Secretary of the Treasury may waive the imposition of the tax imposed under section 4971(b) of the Code in appropriate cases.

.04 Rev. Rul. 79-237, 1979-2 C.B. 190, provides that in the year of termination of a plan, the tax imposed by § 4971(b) applies unless the accumulated funding deficiency, as of the end of the plan year in which the plan is terminated, is reduced to zero.

.05 Rev. Proc. 81-44, 1981-2 C.B. 618, outlines the procedure for requesting a waiver of the tax imposed under § 4971(b).

Section 3. Conditions for Waiver

The tax imposed on an employer under § 4971(b) for failure to meet the minimum funding standards with respect to a defined benefit plan is waived for all applicable years, if the four conditions enumerated below are satisfied:

.01 The plan is subject to Title IV of ERISA and is terminated in a standard termination under section 4041 of ERISA.

.02 Plan participants are not entitled to any portion of residual assets remaining after all liabilities of the plan to participants and their beneficiaries have been satisfied.

.03 Excise taxes that have been or could be imposed under § 4971(a) of the Code have been paid for all taxable years, including the taxable year related to the year of plan termination.

.04 All applicable forms in the 5500 series, including Schedules B (Actuarial Information), have been filed for the plan for all plan years including the year of plan termination.

Section 4. Effective Date

This procedure applies to the excise taxes under § 4971(b) of the Code with respect to plans terminating with termination dates under section 4041 of ERISA that occur on or after January 1, 2000.

Drafting Information

The principal author of this revenue procedure is Bill Kerr of the Tax Exempt and Government Entities Division. For further information regarding this revenue procedure, call Employee Plans Taxpayer Assistance at (202) 622-6076 (not a toll free number) between 2:30 and 3:30 Eastern time, Monday through Thursday. Mr. Kerr's number is (202) 622-8055 (also not a toll free number).

Rev. Rul. 2000-18 Section 1042(e).--Recapture of Gain on Disposition of Qualified Replacement Property

April 3, 2000

ISSUE

Whether the transfer of qualified replacement property to a partnership in exchange for a partnership interest by a taxpayer that has elected to defer the recognition of gain under section 1042(a) of the Internal Revenue Code is a disposition of the qualified replacement property resulting in recapture of the deferred gain under section 1042(e).

FACTS

The taxpayer is a shareholder of Company A, a closely held domestic C corporation. Company A maintains an employee stock ownership plan (ESOP) that satisfies the requirements of section 4975(e)(7). Company A has one class of common stock that constitutes employer securities within the meaning of section 409(l) of the Code. The taxpayer did not receive the shares in a distribution from a plan described in section 401(a), or a transfer pursuant to an option or other right to acquire stock to which section 83, 422 or 423 applied. The taxpayer sells all of the Company A shares to the Company A ESOP and reinvests the proceeds of the sale in qualified replacement property (QRP), as defined in section 1042(c)(4), within 12 months of the date of the sale. The taxpayer makes a timely election under section 1042(a) to defer recognition of the gain realized from the sale of the qualified securities to the ESOP. Under section 1042(d), the basis of the QRP is reduced to reflect the deferred gain on the sale. After the section 1042 election, the taxpayer contributes the QRP to a partnership in exchange for an interest in the partnership.

LAW AND ANALYSIS

Section 1042(a) provides that a taxpayer or executor may elect in certain cases not to recognize long-term capital gain on the sale of "qualified securities" to an employee stock ownership plan (as defined in section 4975(e)(7)) or eligible worker- owned cooperative if the taxpayer purchases "qualified replacement property" (as defined in section 1042(c)(4)) within the replacement period of section 1042(c)(3) and the

requirements of section 1042(b) and section 1.1042-1T of the Temporary Income Tax Regulations are satisfied.

A sale of "qualified securities" meets the requirements of section 1042(b) if: (1) the qualified securities are sold to an employee stock ownership plan (as defined in section 4975(e)(7)) or an eligible worker-owned cooperative; (2) the plan or cooperative owns (after application of 318(a)(4)), immediately after the sale, at least 30 percent of (a) each class of outstanding stock of the corporation (other than stock described in section 1504(a)(4)) which issued the securities or (b) the total value of all outstanding stock of the corporation (other than stock described in section 1504(a)(4)); (3) the taxpayer files with the Secretary a verified written statement of the employer whose employees are covered by the employee stock ownership plan or an authorized officer of the cooperative consenting to the application of sections 4978 and 4979A with respect to such employer or cooperative; and (4) the taxpayer's holding period with respect to the qualified securities is at least three years (determined as of the time of the sale).

Section 1042(c)(1) provides that qualified securities are employer securities (as defined in section 409(l)) which are issued by a domestic C corporation that has no stock outstanding that is readily tradable on an established securities market and were not received by the taxpayer in a distribution from a plan described in section 401(a) or a transfer pursuant to an option or other right to acquire stock to which section 83, 422, or 423 applied (or to which section 422 or 424 (as in effect on the day before the date of the enactment of the Revenue Reconciliation Act of 1990) applied).

The taxpayer must purchase "qualified replacement property" within the "replacement period" which is defined in section 1042(c)(3) as the period which begins 3 months before the date on which the sale of qualified securities occurs and which ends 12 months after the date of such sale.

Section 1042(c)(4)(A) defines "qualified replacement property" as any security issued by a domestic "operating corporation" (as defined in section 1042(c)(4)(B)) which did not, for the taxable year preceding the taxable year in which such security was purchased, have passive investment income (as defined in section 1362(d)(3)(C)) in excess of 25 percent of the gross receipts of such corporation for such preceding taxable year and is not the corporation which issued the qualified securities that such security is replacing or a member of the same controlled group of corporations (within the meaning of section 1563(a)(1)) as such corporation.

Section 1042(d) provides that the basis of the taxpayer in qualified replacement property purchased by the taxpayer during the replacement period is reduced by the amount of gain not recognized by reason of such purchase and the application of section 1042(a). If more than one item of qualified replacement property is purchased, the basis of each of such items is reduced by an amount determined by multiplying the

total gain not recognized by reason of such purchase and the application of subsection (a) by a fraction the numerator of which is the cost of such item of property and the denominator of which is the total cost of all such items of property.

Section 1042(e)(1) states that "if a taxpayer disposes of any qualified replacement property, then, notwithstanding any other provision of this title, gain (if any) shall be recognized to the extent of the gain which was not recognized under subsection (a) by reason of the acquisition by such taxpayer of such qualified replacement property."

The legislative history of section 1042(e) indicates that section 1042(e) was added to coordinate the requirement that deferred gain be recognized on the disposition of any qualified replacement property with other nonrecognition provisions of the Code. "Effective for dispositions made after the date of enactment, the Act overrides all other provisions permitting nonrecognition and requires that gain realized upon the disposition of qualified replacement property be recognized at that time." S. Rep. 99-313, 99th Cong., 2nd Sess., 1032 (1986), 1986-3 C.B., v. 3, 1032. Thus, gain realized from the disposition of any qualified replacement property by a taxpayer who made an election under section 1042 must be recognized at the time of the disposition regardless of any other nonrecognition provisions of the Code that may otherwise be applicable.

Section 721(a) provides that generally no gain or loss is recognized to a partnership or to any of its partners in the case of a contribution of property to the partnership in exchange for an interest in the partnership.

Limited exceptions to the rule of section 1042(e)(1) are provided in section 1042(e)(3) which provides that the recapture rules of section 1042(e)(1) do not apply to any transfer of qualified replacement property that occurs: (1) in any reorganization (within the meaning of section 368) unless the person making the election under section 1042(a)(1) owns stock representing control of the acquiring or acquired corporation and such property is substituted basis property in the hands of the transferee; (2) by reason of the death of the person making the election; (3) by gift; or (4) in any transaction to which section 1042(a) applies.

The contribution of qualified replacement property to a partnership in exchange for an interest in the partnership is not a transfer of qualified replacement property described in any of the exceptions in section 1042(e)(3).

In the present situation, the taxpayer disposed of qualified replacement property by contributing it to a partnership in exchange for an interest in the partnership. Therefore, although a contribution of property to a partnership in exchange for an interest in the partnership is ordinarily a nonrecognition event under section 721, section 1042(e)(1) requires that any gain realized on the contribution be recognized to the extent of the gain that was deferred under section 1042(a).

HOLDING

The transfer of qualified replacement property to a partnership in exchange for a partnership interest by a taxpayer that has elected to defer the recognition of gain under section 1042(a) is a disposition of the qualified replacement property under section 1042(e). Accordingly, under section 1042(e), any gain realized on the disposition is required to be recognized by the taxpayer at the time of the transfer to the extent of the gain that was not recognized under section 1042(a) by reason of the acquisition by the taxpayer of the qualified replacement property.

EFFECT ON OTHER REVENUE RULING(S): N/A

PROSPECTIVE APPLICATION: N/A

DRAFTING INFORMATION

The principal author of this revenue ruling is John Ricotta of the Associate Chief Counsel (Employee Benefits & Exempt Organizations) (CC:EBEO:Br5). For Further information regarding this revenue ruling contact John Ricotta on (202) 622-4290 (not a toll-free call).

Part III. --- Administrative, Procedural, and Miscellaneous

Weighted Average Interest Rate Update

Notices 97-56, 97-69, 97-74, 98-9, 98-15, 98-18, 98-26, 98-32, 98-33, 98-37, 98-44, 98-48, 98-51, 98-56, 98-64, 99-7, 99-11, 99-15, 99-21, 99-28, 99-33, 99-38, 99-39, 99-49, 99-52, 99-54, 99-61, 2000-8, 2000-2, 2000-18, 2000-25, 2000-27, 2000-31, 2000-40, 2000-46, 2000-42

Notice 88-73 provides guidelines for determining the weighted average interest rate and the resulting permissible range of interest rates used to calculate current liability for the purpose of the full funding limitation of ' 412(c)(7) of the Internal Revenue Code as amended by the Omnibus Budget Reconciliation Act of 1987 and as further amended by the Uruguay Round Agreements Act, Pub. L. 103-465 (GATT).

Average Yield On 30-Year Treasury Constant Maturities

Month	Percent	Month	Percent	Month	Percent
September 1997	6.50	September 1998	5.20	September 1999	6.07
October 1997	6.33	October 1998	5.01	October 1999	6.26
November 1997	6.11	November 1998	5.25	November 1999	6.15
December 1997	5.99	December 1998	5.06	December 1999	6.35
January 1998	5.81	January 1999	5.16	January 2000	6.63
February 1998	5.89	February 1999	5.37	February 2000	6.23
March 1998	5.95	March 1999	5.58	March 2000	6.05
April 1998	5.92	April 1999	5.55	April 2000	5.85
May 1998	5.93	May 1999	5.81	May 2000	6.15
June 1998	5.70	June 1999	6.04	June 2000	5.93
July 1998	5.68	July 1999	5.98	July 2000	5.85
August 1998	5.54	August 1999	6.07	August 2000	5.72

EMPLOYEE PLANS CPE TECHNICAL TOPICS FOR 2001

The following rates were determined for the plan years beginning in the month shown below.

Month	Weighted Average	90% to 107% Permissible Range	90% to 110% Permissible Range
October 1997	6.83	6.14 to 7.30	6.14 to 7.51
November 1997	6.81	6.13 to 7.29	6.13 to 7.49
December 1997	6.79	6.11 to 7.47	6.11 to 7.76
Month	Weighted Average	90% to 106% Permissible Range	90% to 110% Permissible Range
January 1998	6.77	6.09 to 7.17	6.09 to 7.44
February 1998	6.73	6.06 to 7.14	6.06 to 7.41
Month	Weighted Average	90% to 106% Permissible Range	90% to 110% Permissible Range
March 1998	6.71	6.04 to 7.11	6.04 to 7.38
April 1998	6.67	6.00 to 7.07	6.00 to 7.34
May 1998	6.63	5.97 to 7.03	5.97 to 7.29
June 1998	6.59	5.93 to 6.99	5.93 to 7.25
July 1998	6.55	5.90 to 6.95	5.90 to 7.21
August 1998	6.51	5.86 to 6.90	5.86 to 7.16
September 1998	6.46	5.82 to 6.85	5.82 to 7.11
October 1998	6.40	5.76 to 6.79	5.76 to 7.05
November 1998	6.34	5.71 to 6.72	5.71 to 6.72
December 1998	6.29	5.66 to 6.67	5.66 to 6.92
Month	Weighted Average	90% to 105% Permissible Range	90% to 110% Permissible Range
January 1999	6.24	5.62 to 6.55	5.62 to 6.87
February 1999	6.29	5.57 to 6.50	5.57 to 6.81
March 1999	6.15	5.54 to 6.46	5.54 to 6.77
April 1999	6.11	5.50 to 6.42	5.50 to 6.72
May 1999	6.17	5.46 to 6.38	5.46 to 6.68
June 1999	6.04	5.44 to 6.34	5.44 to 6.65
July 1999	6.03	5.43 to 6.33	5.43 to 6.63
August 1999	6.01	5.41 to 6.31	5.41 to 6.61

EMPLOYEE PLANS CPE TECHNICAL TOPICS FOR 2001

September 1999	6.00	5.40 to 6.30	5.40 to 6.60
October 1999	6.09	5.39 to 6.29	5.39 to 6.59
November 1999	5.99	5.39 to 6.29	5.39 to 6.59
December 1999	5.90	5.40 to 6.30	5.40 to 6.60
January 2000	6.01	5.41 to 6.31	5.41 to 6.61
February 2000	6.03	5.43 to 6.34	5.43 to 6.64
March 2000	6.04	5.44 to 6.34	5.44 to 6.64
April 2000	6.03	5.43 to 6.33	5.43 to 6.64
May 2000	6.02	5.41 to 6.32	5.41 to 6.62
June 2000	6.01	5.41 to 6.31	5.41 to 6.61
July 2000	5.99	5.39 to 6.29	5.39 to 6.59
August 2000	5.98	5.38 to 6.28	5.38 to 6.57
September 2000	5.96	5.36 to 6.26	5.36 to 6.56